H.R. 5551 AND H.R. 6086

HEARINGS

BEFORE THE

SUBCOMMITTEE ON SBA AND SBIC AUTHORITY, MINORITY ENTERPRISE AND GENERAL SMALL BUSINESS PROBLEMS

OF THE

COMMITTEE ON SMALL BUSINESS HOUSE OF REPRESENTATIVES

NINETY-SEVENTH CONGRESS

SECOND SESSION

WASHINGTON, D.C., APRIL 28 AND 29, 1982

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H.R. 5551 and H.R. 6086

WEDNESDAY, APRIL 28, 1982

HOUSE OF REPRESENTATIVES, SUBCOMMITTEE ON SBA AND SBIC AUTHORITY, MINORITY ENTERPRISE AND GENERAL SMALL BUSINESS PROBLEMS, COMMITTEE ON SMALL BUSINESS,

Washington, D.C.

The subcommittee met, pursuant to notice, at 9 a.m., at 2359-A Rayburn House Office Building, Washington, D.C., Hon. Parren J. Mitchell (chairman of the subcommittee) presiding.

Mr. MITCHELL. Good morning. This hearing is now in order.

OPENING STATEMENT OF CHAIRMAN MITCHELL

Mr. MITCHELL. This morning's hearing concerns two bills: H.R. 5551 which basically would require a 45-day leadtime between the publication of notice of a pending Federal procurement and issuance of the contract; and H.R. 6086, which changes certain SBA program levels, requires that SBA fully utilize its programs and keep a record of applicants, prohibits SBA from refusing to issue guarantees on pollution bonds simply because the project involves industrial revenue bond financing, prohibits SBA from arbitrarily refusing to approve surety bond guarantees on contracts eligible under statutory provisions, codifies existing regulations on guaranteed loan interest rates, and requires SBA to follow the Administrative Procedure Act if it revises its size standards.

In addition, in accord with the committee's decision of last March to channel the limited amount of SBA direct loans to areas of high unemployment, we have drafted legislation to carry out this decision.

As a result of preliminary comments on these proposals, some revisions have been made and the proposals have been consolidated into a committee print dated April 27.

[H.R. 5551, H.R. 6086, and the committee print referred to above follow:]

I

97TH CONGRESS
2D SESSION

H. R. 5551

To amend section 8(e) of the Small Business Act to improve small business access to Federal procurement information.

IN THE HOUSE OF REPRESENTATIVES

FEBRUARY 22, 1982

Mr. MITCHELL of Maryland (for himself and Mr. IRELAND) introduced the following bill; which was referred jointly to the Committees on Government Operations and Small Business

---

A BILL

To amend section 8(e) of the Small Business Act to improve small business access to Federal procurement information.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 8(e) of the Small Business Act is amended by adding at the end thereof the following new sentence: "Whenever a procuring agency is required to publish notice of procurement actions, it shall (1) issue a solicitation for a procurement action only after at least fifteen days have elapsed from the date of publication of a proper notice of the action; and (2) shall foreclose competition under a procurement action only after at least thirty days have elapsed from

the date of issuance of the solicitation, or, in the case of orders under a basic agreement, basic ordering agreement, or similar arrangement, the date of publication of a proper notice of intent to place the order.".

I

97TH CONGRESS
2D SESSION

H.R. 6086

To amend the Small Business Act and the Small Business Investment Act of 1958.

IN THE HOUSE OF REPRESENTATIVES

APRIL 6, 1982

Mr. MITCHELL of Maryland introduced the following bill; which was referred to the Committee on Small Business

---

A BILL

To amend the Small Business Act and the Small Business Investment Act of 1958.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. Section 20 of the Small Business Act is amended as follows:

(a) by striking from paragraph (2) of subsection (n) the figure "$60,000,000" and by inserting in lieu thereof "$167,000,000";

(b) by striking from paragraph (3) of subsection (n) the figure "$35,000,000" and by inserting in lieu thereof "$41,000,000" and by striking from such para-

graph the figure "$160,000,000" and by inserting in lieu thereof "$250,000,000";

(c) by striking from paragraph (2) of subsection (q) the figure "$60,000,000" and by inserting in lieu thereof "$167,000,000"; and

(d) by striking from paragraph (3) of subsection (q) the figure "$35,000,000" and inserting in lieu thereof "$41,000,000" and by striking from such paragraph the figure "$160,000,000" and by inserting in lieu thereof "$250,000,000".

SEC. 2. Section 5(b) of the Small Business Act is amended as follows:

(a) by striking "and" at the end of paragraph (10);

(b) by striking the period at the end of paragraph (11) and by inserting ";"; and

(c) by adding the following new paragraph:

"(12) Notwithstanding any other provision of law, the Administration shall enter into commitments to guarantee loans, debentures, payment of rentals or other amounts due under qualified contracts and other types of financial assistance and to enter commitments to guarantee sureties against loss pursuant to programs under this Act and the Small Business Investment Act of 1958 in the full amounts provided by law subject only to (A) the availability of qualified applica-

tions for such guarantees and (B) limitations contained in appropriation Acts. Nothing in this paragraph authorizes the Administration to reduce or limit its authority to enter commitments for such guarantees to qualified applicants.".

SEC. 3. Section 404(b) of the Small Business Investment Act of 1958 is amended as follows:

(a) by striking from paragraph (1) thereof "may be issued" and by inserting in lieu thereof "shall be issued"; and

(b) by striking the period at the end of paragraph (1) thereof and by inserting in lieu thereof ", and the Administration is expressly prohibited from denying such guarantee when the property is so acquired.".

SEC. 4. Section 411 of the Small Business Investment Act of 1958 is amended by adding the following at the end of subsection (h): "The Administration shall not establish eligibility criteria based on the amount of the bond, subject to the limitation in subsections (a) and (c), or upon a percentage related to previously successfully completed contracts. The Administration shall evaluate each application on a case-by-case basis and based thereon shall determine the appropriate guarantee.".

SEC. 5. Section 7 of the Small Business Act is amended by striking from paragraph (4) of subsection (a) "shall not exceed a rate prescribed by the Administration, and the rate

of interest" and by inserting the following: "shall not exceed a rate—

"(A) equal to the New York prime rate on the date the loan proceeds are disbursed plus, in the discretion of the lender, up to, but not more than, two and one-quarter percentage points if the loan has a maturity under seven years; and

"(B) equal to the New York prime rate on the date the loan proceeds are disbursed plus, in the discretion of the lender, up to, but not more than, two and three-quarter percentage points if the loan has a maturity of seven years or more.

The rate of interest.".

SEC. 6. Section 10 of the Small Business Act is amended by adding the following new subsection:

"(h) The Administration shall maintain a record of all applications for or inquiries about the availability of funding for financial assistance under this Act and for guarantees under the Small Business Investment Act of 1958. Such record shall include the name, address, and telephone number of the applicant or person inquiring and the dollar amount involved and shall be kept for a period of at least one year from the date of each.".

SEC. 7. Section 5(b) of the Small Business Act is amended by adding the following new paragraphs:

"(13) The Administration shall notify the Senate Small Business Committee and the Small Business Committee of the United States House of Representatives before reprograming any program amounts authorized in appropriations Acts or reports explanatory thereof and shall notify the Senate Small Business Committee and the Small Business Committee of the United States House of Representatives before implementing any reorganization of such agency.".

SEC. 8. Section 2 of the Small Business Act is amended by striking "section 7(i)" from paragraph (1) of subsection (c) and by inserting "section 7(a)(11)".

SEC. 9. Section 7 of the Small Business Act is amended as follows:

(a) by striking, wherever it appears therein, "section 7(i)" from paragraphs (1), (2), (3), (8), (9), and (11) of subsection (j) and by inserting "section 7(a)(11)";

(b) by striking from subsection (k) "section 7(i)" and by inserting "section 7(a)(11)";

(c) by striking subsections (e), (h), (i), and (l); and

(d) by striking all of subsection (c) after the first two sentences in subparagraph (D) of paragraph (4) and inserting the following: "Such loans, subject to the reductions required by subparagraphs (A) and (B) of paragraph 7(b)(1), shall be in amounts equal to 100 percent of loss if the applicant is a homeowner and 85

percent of loss if the applicant is a business or otherwise. The interest rates for loans made under paragraphs 7(b) (1) and (2), as determined pursuant to this paragraph (4), shall be the rate of interest which is in effect on the date the disaster commenced: *Provided,* That no loan under paragraphs 7(b) (1) and (2) shall be made, either directly or in cooperation with banks or other lending institutions through agreements to participate on an immediate or deferred (guaranteed) basis, if the total amount outstanding and committed to the borrower under subsection 7(b) would exceed $500,000 for each disaster unless an applicant constitutes a major source of employment in an area suffering a disaster, in which case the Administration, in its discretion, may waive the $500,000 limitation.".

SEC. 10. Section 3(a) of the Small Business Act is amended by striking "enterprises that are engaged in the business of production of food and fiber, ranching and raising of livestock, aquaculture, and all other farming and agricultural related industries" and by inserting "agricultural enterprises".

SEC. 11. Section 3(h) of the Small Business Act is amended as follows:

(a) by striking "availability of credit" and by inserting "availability of sufficient credit"; and

(b) by striking "conditions" and by inserting "conditions and at reasonable rates,".

SEC. 12. Section 3 of the Small Business Act is amended by adding the following new subsection:

"(j) For purposes of this Act, the term "agricultural enterprises" means enterprises which are engaged in the business of production of food and fiber, ranching and raising of livestock, aquaculture, and all other farming and agricultural related industries.".

SEC. 13. Section 18 of the Small Business Act is amended as follows:

(a) by striking subsection (b) and by striking the designation of subsection (a); and

(b) by striking "those enterprises engaged in the production of food and fiber, ranching, and raising of livestock, aquaculture, and all other farming and agricultural related industries" and by inserting "agricultural enterprises".

SEC. 14. Section 3 of the Small Business Act is amended by striking from subsection (a) "*Provided*, That the Administration shall not promulgate, amend, or rescind any rule regulation with respect to size standards prior to March 31, 1981." and inserting in lieu thereof the following: "*Provided*, That notwithstanding the waiver provisions of section 553 of title 5 of the United States Code, the Administration shall

not promulgate, amend or rescind any rule or regulation with respect to size standards except in accordance with the procedures of chapter 5 of title 5, United States Code.".

SEC. 15. This Act shall take effect October 1, 1983: *Provided*, That the amendments made by sections 9(d) and 10 through 13 shall not apply to any disaster which commenced on or before July 2, 1980.

[COMMITTEE PRINT]

APRIL 27, 1982

97TH CONGRESS
2D SESSION

H.R.

To amend the Small Business Act and the Small Business Investment Act of 1958.

IN THE HOUSE OF REPRESENTATIVES

APRIL , 1982

Mr. MITCHELL of Maryland introduced the following bill; which was referred to the Committee on

---

A BILL

To amend the Small Business Act and the Small Business Investment Act of 1958.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

(identical to § 1 of H.R. 6086)

SECTION 1. Section 20 of the Small Business Act is amended as follows:

(a) by striking from paragraph (2) of subsection (n) the figure "$60,000,000" and by inserting in lieu thereof "$167,000,000";

(b) by striking from paragraph (3) of subsection (n) the figure "$35,000,000" and by inserting in lieu thereof "$41,000,000" and by striking from such paragraph the figure "$160,000,000" and by inserting in lieu thereof "$250,000,000";

(c) by striking from paragraph (2) of subsection (q) the figure "$60,000,000" and by inserting in lieu thereof "$167,000,000"; and

(d) by striking from paragraph (3) of subsection (q) the figure "$35,000,000" and inserting in lieu thereof "$41,000,000" and by striking from such paragraph the figure "$160,000,000" and by inserting in lieu thereof "$250,000,000".

(technical revision of § 2 of H.R. 6086)

SEC. 2. Section 5 of the Small Business Act is amended by adding the following new subsection:

"(f) Notwithstanding any other provision of law, the Administration shall enter into commitments for direct loans and to guarantee loans, debentures, payment of rentals or other amounts due under qualified contracts and other types of financial assistance and to enter commitments to guarantee sureties against loss pursuant to programs under this Act and

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the Small Business Investment Act of 1958 in the full amounts provided by law subject only to (1) the availability of qualified applications for such guarantees and (2) limitations contained in appropriation Acts. Nothing in this subsection authorizes the Administration to reduce or limit its authority to enter commitments for direct loans or for such guarantees to qualified applicants.".

(identical to § 3 of H.R. 6086)

SEC. 3. Section 404(b) of the Small Business Investment Act of 1958 is amended as follows:

(a) by striking from paragraph (1) thereof "may be issued" and by inserting in lieu thereof "shall be issued"; and

(b) by striking the period at the end of paragraph (1) thereof and by inserting in lieu thereof ", and the Administration is expressly prohibited from denying such guarantee when the property is so acquired.".

(identical to § 4 of H.R. 6086)

SEC. 4. Section 411 of the Small Business Investment Act of 1958 is amended by adding the following at the end of subsection (h): "The Administration shall not establish eligibility criteria based on the amount of the bond, subject to the limitation in subsections (a) and (c), or upon a percentage related to previously successfully completed contracts. The Administration shall evaluate each application on a case-by-

case basis and based solely thereon shall determine the appropriate guarantee.".

(revision of § 5 of H.R. 6086)

SEC. 5. Section 7 of the Small Business Act is amended by striking from paragraph (4) of subsection (a) "reasonable but shall not exceed a rate prescribed by the Administration, and the rate of interest" and by inserting the following: "reasonable. Subject to the approval of the Administration, a participating lending institution may establish such rate of interest on guaranteed loans and on its share of immediate participation loans: *Provided,* That the Administration shall not require that the rate be less than a rate—

"(A) equal to the lowest New York prime rate plus, in the discretion of the lender, two and one-quarter percentage points if the loan has a maturity under seven years; or

"(B) equal to the lowest New York prime rate plus, in the discretion of the lender, two and three-quarters percentage points if the loan has a maturity of seven years or more.

The rate of interest.".

(minor revision of § 6 of H.R. 6086)

SEC. 6. Section 10 of the Small Business Act is amended by adding the following new subsection:

"(h) The Administration shall maintain a record of all applications for or inquiries about the availability of funding for financial assistance under this Act and for guarantees and purchases under the Small Business Investment Act of 1958. Such record shall include the name, address, and telephone number of the applicant or person inquiring and the dollar amount involved and shall be kept for a period of at least one year from the date of each.".

(technical revision of § 7 of H.R. 6086)

SEC. 7. Section 5 of the Small Business Act is amended by adding the following new subsection:

"(g) The Administration shall notify the Senate Small Business Committee and the Small Business Committee of the United States House of Representatives before reprograming any program amounts authorized in appropriations Acts or reports explanatory thereof and shall notify the Senate Small Business Committee and the Small Business Committee of the United States House of Represe tatives before implementing any reorganization of such agency.".

(identical to § 8 of H.R. 6086)

SEC. 8. Section 2 of the Small Business Act is amended by striking "section 7(i)" from paragraph (1) of subsection (c) and by inserting "section 7(a)(11)".

(identical to § 9 of H.R. 6086)

SEC. 9. Section 7 of the Small Business Act is amended as follows:

(a) by striking, wherever it appears therein, "section 7(i)" from paragraphs (1), (2), (3), (8), (9), and (11) of subsection (j) and by inserting "section 7(a)(11)";

(b) by striking from subsection (k) "section 7(i)" and by inserting "section 7(a)(11)";

(c) by striking subsections (e), (h), (i), and (l); and

(d) by striking all of subsection (c) after the first two sentences in subparagraph (D) of paragraph (4) and inserting the following: "Such loans, subject to the reductions required by subparagraphs (A) and (B) of paragraph 7(b)(1), shall be in amounts equal to 100 per centum of loss if the applicant is a homeowner and 85 per centum of loss if the applicant is a business or otherwise. The interest rates for loans made under paragraphs 7(b) (1) and (2), as determined pursuant to this paragraph (4), shall be the rate of interest which is in effect on the date the disaster commenced: *Provided*, That no loan under paragraphs 7(b) (1) and (2) shall be made, either directly or in cooperation with banks or other lending institutions through agreements to participate on an immediate or deferred (guaranteed) basis, if the total amount outstanding and committed to the borrower under subsection 7(b) would exceed $500,000

for each disaster unless an applicant constitutes a major source of employment in an area suffering a disaster, in which case the Administration, in its discretion, may waive the $500,000 limitation.".

(new high unemployment area direct loans)

SEC. 10. Section 7(a) of the Small Business Act is amended by adding the following new paragraph:

"(16)(A) No direct loan may be made pursuant to this subsection unless the Administration determines—

"(i) that the applicant for such loan (whether a startup or existing small business concern) demonstrates a potential for sustained business growth as evidenced by (I) a capacity to create, expand, or satisfy domestic or international markets for the products or services produced or rendered by such applicant, (II) location in a geographic area suitable for its business operations and access to markets, and (III) lack of unduly restrictive agreements which, if exercised, could substantially impede the profitable operations of the applicant;

"(ii) that the applicant has given reasonable assurance that it will create employment opportunities within a two-year period after all loan proceeds are disbursed; and

"(iii) those managerial or marketing weaknesses which exist with respect to such applicant and devises, in concert with the applicant, a management plan, prior to the disbursement of any proceeds of such loan, to address such weaknesses. Such plan, if needed, shall be in writing, provide for identifiable business goals, plans of action and timetables for accomplishments, and shall be incorporated by reference into the loan authorization agreement. The Administration shall provide assistance for the implementation of such plans on a priority basis through such management and technical assistance activities as are authorized by this Act.

"(B) Direct loan funds under subsection (a) shall be allocated to the Administration's regional offices at least quarterly each fiscal year. The amount of such allocation shall be based solely upon the average total number of unemployed workers residing within each regional area as a percent of the average total unemployed work force nationwide for the immediately preceding fiscal quarter, or for the most recent fiscal quarter for which such statistics are available. Each regional office shall allocate such funds to each district office within its jurisdiction at least quarterly based solely upon the average total number of unemployed workers residing within the district as a percent of the average total unemployed work force regionwide for the immediately preceding fiscal

quarter, or for the most recent fiscal quarter for which such statistics are available. During the last fifteen calendar days of each fiscal year quarter the Administration may reallocate direct loan funds among its regions or districts if it is unreasonable to expect that such region or district will commit substantially all of its allocation before the expiration of such quarter.

"(C) Direct loans authorized by this subsection shall be extended on a priority basis within each of the Administration's designated district areas to those qualified applicants in order of the following priority—

"(i) those applicants which (I) satisfy the requirements of subparagraph (A), (II) are located in a labor surplus area (as defined pursuant to Defense Manpower Policy 4B (32A CFR chapter 1) or any successor policy), (III) agree to perform or render a substantial proportion of its production or services within such areas, and (IV) will utilize the loan proceeds solely for construction, renovation, or the purchase of land, buildings, machinery, or equipment;

"(ii) those applicants which satisfy the requirements of subparagraph (A) of subparagraph (C)(i) (I), (II), and (III); and

"(iii) those applicants which satisfy the requirements of subparagraph (A).

"(D) This paragraph shall not apply to direct loans made pursuant to paragraph (10) of this subsection.".

(new high unemployment area direct loans—matching funds)

SEC. 11. Section 7(a)(3) of the Small Business Act is amended to read as follows:

"(3)(A) No loan under this subsection shall be made if the total amount outstanding and committed (by participation or otherwise) to the borrower from the business loan and investment fund established by section 4(c)(1) of this Act would exceed $500,000: *Provided,* That the Administration's share of any loan made or effected either directly or in cooperation with banks or other lending institutions through agreements to participate on an immediate basis shall not exceed $350,000: *Provided further,* That any loan made directly pursuant to this subsection shall be accompanied by a injection of additional funds derived from non-Federal sources in the following amounts:

"(1) if the loan is under $100,000 in amount, at least 10 per centum;

"(2) if the loan is between $100,000 and $200,000 in amount, at least 20 per centum; and

"(3) if the loan is over $200,000 in amount, at least 30 per centum.

"(B) The percentages specified in subparagraphs (A) (2) and (3) shall be reduced to 10 per centum and 15 per centum,

respectively, if the non-Federal source funds are derived from a State or local government, including tax-exempt obligations of such governments.

"(C) The Administration shall delegate to each district office the authority to approve direct loans in the amounts specified in subparagraph (A) (1), (2), and (3) under the conditions specified in this Act without seeking higher approval within the Administration.

"(D) For purposes of this paragraph the term 'non-Federal sources' shall include, but not be limited to, State and local government funds (including the proceeds from tax-exempt obligations of such governments), and funds derived from private financial institutions or private equity sources. In no event shall such term include funds derived directly from any grant or loan made, guaranteed, or insured by the Federal Government.".

(new labor surplus area procurement)

SEC. 12. Section 15 of the Small Business Act is amended by striking subsections (d), (e), and (f) and inserting in lieu thereof the following:

"(d) For purposes of this section priority shall be given to the awarding of contracts and the placement of subcontracts to small business concerns which shall perform a substantial proportion of the production on those contracts and subcontracts within areas of concentrated unemployment or

underemployment or within labor surplus areas. Notwithstanding any other provision of law, total labor surplus area set-asides pursuant to Defense Manpower Policy Numbered 4 (32A CFR chapter 1) or any successor policy shall be authorized if the head of the procuring Federal agency or his designee specifically determines that there is a reasonable expectation that offers will be obtained from a sufficient number of eligible concerns so that awards will be made at reasonable prices. As soon as practicable and to the extent possible, in determining labor surplus areas, consideration shall be given to those persons who would be available for employment where suitable employment is available. Until such definition reflects such number, the present criteria of such policy shall govern.

"(e) In carrying out small business set-aside programs, Federal agencies shall award contracts, and encourage the placement of subcontracts for procurement to the following in the manner and in the order stated:

"(1) concerns which are small business concerns and which are located in labor surplus areas, on the basis of a total small business-labor surplus area set-aside;

"(2) concerns which are small business concerns, on the basis of a total small business set-aside;

"(3) concerns which are small business concerns and which are located in a labor surplus area, on the basis of a partial small business-labor surplus area set-aside; and

"(4) concerns which are small business concerns, on the basis of a partial small business set-aside.

"(f) After priority is given to the small business concerns specified in subsection (e), priority also shall be given to the awarding of contracts and the placement of subcontracts, on the basis of a total labor surplus area set-aside, to business concerns which will perform a substantial proportion of the production on those contracts and subcontracts within areas of concentrated unemployment or underemployment or within labor surplus areas.".

(identical to H.R. 5551)

SEC. 13. Section 8(e) of the Small Business Act is amended by adding at the end thereof the following new sentence: "Whenever a procuring agency is required to publish notice of procurement actions, it (1) shall issue a solicitation for a procurement action only after at least fifteen days have elapsed from the date of publication of a proper notice of the action; and (2) shall foreclose competition under a procurement action only after at least thirty days have elapsed from the date of issuance of the solicitation, or, in the case of orders under a basic agreement basic ordering agreement, or

similar arrangement, the date of publication of a proper notice of intent to place the order.".

(identical to §11 of H.R. 6086)

SEC. 14. Section 3(h) of the Small Business Act is amended as follows:

(a) by striking "availability of credit" and by inserting "availability of sufficient credit"; and

(b) by striking "conditions" and by inserting "conditions and at reasonable rates,".

(indentical to § 14 of H.R. 6086)

SEC. 15. Section 3 of the Small Business Act is amended by striking from subsection (a) "*Provided*, That the Administration shall not promulgate, amend, or rescind any rule regulation with respect to size standards prior to March 31, 1981." and inserting in lieu thereof the following: "*Provided*, That notwithstanding the waiver provisions of section 553 of title 5 of the United States Code, the Administration shall not promulgate, amend, or rescind any rule or regulation with respect to size standards except in accordance with the procedures of chapter 5 of title 5, United States Code.".

(Technical revision of § 15 of H.R. 6086)

SEC. 16. This Act shall take effect October 1, 1982: *Provided*, That the amendments made by sections 9(d) and 14 shall not apply to any disaster which commenced on or before July 2, 1980.

(New Sunset of guaranteed loan interest rates)

SEC. 19. Section 5 of this Act is hereby repealed October 1, 1984.

Mr. MITCHELL. I am delighted that Congressman Addabbo is here with us and I will turn to him for an opening statement.

Mr. ADDABBO. Thank you very much, Mr. Chairman.

OPENING STATEMENT OF HON. JOSEPH P. ADDABBO, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW YORK

Mr. ADDABBO. Mr. Chairman, these hearings are the next step toward resolving a number of problems experienced by small businesses. I would like to take this opportunity to comment on the committee print of April 27, 1982, which I understand will be introduced today by the chairman. It contains identical language to previous bills (H.R. 6086, and H.R. 5551) and includes new provisions regarding direct loans and labor surplus areas. As cosponsor, I see it as an acceptable compromise which deals with many of the issues brought before our committee over the last year, and I strongly urge the members to support it.

As a longtime member of the Small Business Committee, I have consistently been an enthusiastic supporter of direct loans to small businesses because they simply are not treated like large businesses when they go to a bank for a loan. The New York Times article of April 25, 1982—this past Sunday—is yet another tale of small firms being told that they are simply too small to merit consideration by banks. Even businesses with adequate credit histories are being denied loans if the loan is too small in amount for banks to deal with. In addition, small firms cannot afford to pay interest at several points over the prime rate. All of these factors point to the conclusion that SBA should not only provide loan guarantees to banks for small business loans, but must also provide direct loan assistance. The bill submitted yesterday would continue the direct loan program, but would correct the problems found by the committee caused by bad loan making policy on the part of the Small Business Administration.

I look forward to hearing from all of the witnesses today, and I would like to welcome Ron Peterson, of Pitkin Manufacturing. Mr. Peterson is representing the National Tooling and Machining Association. Over the years, he has experienced problems doing business with the Government which are not unlike those of many small businesses. Also, a welcome to Mr. Burns, of Minority Equity Capital Co., Inc. Thank you both for coming down from New York and taking time out of your busy schedules. I look forward to hearing your testimony today, and only hope that my other duties as chairman of the Defense Appropriations Subcommittee do not require that I leave before you have an opportunity to speak. In any case, I look forward to reading your written testimony.

Following are my comments on specific provisions of the clean bill:

UNSPENT MONEY AT SBA

For years, I have challenged SBA's practice of not spending appropriated funds because of their lack of commitment to some programs. It should not be within SBA's discretion to shirk its program responsibilities merely because it does not like a program passed by Congress for the benefit of small businesses. The last

time SBA was before this committee, its excuse for not spending direct and guarantee loan authority was lack of demand. However, when pressed, SBA could not document any appreciable decrease in demand which would account for this failure to make more loans. Section 2 would require SBA to spend subject only to availability of qualified applications and appropriations limitations. In addition, section 6 also requires SBA to maintain a record of all applications for, or inquiries about, availability of funding for loans and for guarantees. This way, SBA will not be able to claim lack of demand without proving it.

DIRECT LOANS

The new direct loan plan tightens up the program so that SBA will be prevented from making bad loans. The SBA must determine that the loan applicant demonstrates a potential for growth, and that the loan applicant has given reasonable assurance that it will create employment opportunities within a 2-year period. Also, for the first time, SBA must assist direct loan recipients in developing a management plan after loan approval but before disbursement, to help correct any possible management deficiencies. These new requirements and others will assure taxpayers that only firms capable of repaying loans will receive them, and that the economy will benefit from such loan assistance.

Direct loans will be allocated on the basis of unemployment within the region and district, but it should be stressed that all regions and districts will receive direct loan money. However, within each district a priority is given to labor surplus areas and to businesses seeking to fund hard capital expenditures. Also, matching funds will be encouraged from State and local governments.

SBA districts and regions will still have the flexibility to spend the money where the immediate need is. This should give SBA no excuse for not spending appropriated money.

SURETY BONDS

The surety bond program at SBA is vital to the survival of those businesses which are at the mercy of overly cautious bonding policies. Section 4 of the committee print restrains SBA from discriminating against those small firms which, because of fast growth, can demonstrate the ability to complete a contract much larger than any previously completed contracts. This might be a simple way to make a program decision, but it simply is not fair, and it prevents small firms from growing any faster than SBA thinks the firm should grow.

COMMERCE BUSINESS DAILY

In previous hearings, we received testimony that many small firms never had the opportunity to compete for Federal contracts because they never got adequate notice of the solicitation. Section 13, which is identical to H.R. 5551, would require that a minimum period of time elapse between publication in the CBD and issuance of the solicitation, and from issuance of the solicitation and bid

opening or proposal acceptance. The agencies already operate under regulations to this effect, but this apparently is insufficient.

REORGANIZATION OF SBA AND REPROGRAMING

We have heard that the administration is considering a transfer of program responsibilities from SBA to the Department of Commerce. In addition, SBA asks the Appropriations Committee for reprogramings without adequate notice to this committee. Section 7 requires SBA to notify this committee of these actions so that we can discharge our duties.

LABOR SURPLUS PROCUREMENT

Section 12 corrects some of the confusion about the priority given to firms under the labor surplus area preference set forth in the Small Business Act. It also would have the effect of promoting greater uniformity in the Federal acquisition system by removing the existing prohibition disallowing DOD to participate in total labor surplus area set-asides.

Mr. MITCHELL. Thank you very much, Congressman Addabbo.

Before we start with the witnesses, I would like to suggest a format. We have many persons who want to testify, and I think we have received statements from many of them. So, as we proceed, witnesses, if they so desire, may submit their entire statement for the record and simply speak to the highlights or, if they so desire, read their entire statement. Either approach is all right with me. But we do have a very, very large number of people who want to testify and we want to hear from all of them.

I am delighted that Bernie Berkowitz is here in another capacity. Bernie Berkowitz is from Charm City, which is Baltimore, and which is my city. I must say that in the years that I have worked with him I have been very so impressed by his zealous concern for small business and minority businesses. I have been significantly impressed by the number of occasions on which he has really gone out on a limb to do the right thing. He has taken a little bit of flak on occasion, but generally has been vindicated.

You are here in another capacity, Mr. Berkowitz, and we are delighted that you are here. I prefer to recognize you as the key person in BEDCO, the Baltimore Economic Development Corp., but we will indicate that you are representing the Council of Pollution Control Financing Agencies. If you will come right up and give your statement, we would be delighted.

I started to ask you how everything was in the city, but I just left there at 7 o'clock this morning, so everything is all right. Thank you again for being here.

TESTIMONY OF BERNARD BERKOWITZ, PRESIDENT, BALTIMORE ECONOMIC DEVELOPMENT CORP., ON BEHALF OF THE COUNCIL OF POLLUTION CONTROL FINANCING AGENCIES

Mr. BERKOWITZ. Thank you, Mr. Chairman, for those very kind words.

Mr. Chairman, members of the committee, I am Bernard Berkowitz, president of the Baltimore Economic Development Corp. and a member of the Council of Pollution Control Financing Agen-

cies. The Council is a nonprofit organization formed by State and local agencies which serve as issuers of tax-exempt financings for pollution control and solid waste facilities. The Council includes associate members from financial, legal, and industrial sectors. Council members have been active in supporting the continued availability of tax-exempt financing as an important part of the Nation's efforts to achieve environmental goals and foster a sustained economic recovery.

Before I continue with the prepared remarks concerning H.R. 6086 and the council's views, I would like to take a moment to acknowledge the tremendous help that Baltimore City has received through the efforts of Congressman Parren Mitchell in the form of projects that the Congressman has supported, in the form of legislation that has been helpful to Baltimore City and to the other distressed cities around the country, and in the form of legislative assistance, to small and minority businesses and in many, many other ways.

On behalf of Mayor Schaefer, I want to again express our appreciation for the invaluable assistance that we have received over the years from your efforts.

Mr. MITCHELL. Thank you.

Mr. BERKOWITZ. I also want to say that I have a longstanding friendship with Congressman Mitchell that goes back, I guess, at least 15 years to the days when the Congressman was heading the Community Action Agency in Baltimore and that friendship is highly valued and we have had some good times together.

Mr. MITCHELL. We sure have.

Mr. BERKOWITZ. Secondly, although I am not here on behalf of the city, I do want to say that the city strongly supports other aspects of H.R. 6086, in particular the amendments that deal with additional authorizations, funding for the equal opportunity loan program, for MESBIC's, for SBIC's, and as one of my colleagues at BEDCO, Larry Smith, will later testify to, our support for the SBA 503 program, which is very important to us.

On behalf of the Council, I welcome this opportunity to provide the committee with our views regarding H.R. 6086 and the overall dire circumstance surrounding the availability of tax-exempt pollution control financing. This committee is to be commended for its continuing efforts to help navigate small business through these troubled economic waters. H.R. 6086 personifies this deep-seated concern for small business, the largest source of new jobs and economic activity in the Nation.

The administration has proposed several changes to current tax policy it believes will reduce the growth in the volume of pollution control bonds. Additionally, during the past year, the administration made preemptive administrative decisions that struck deep into the functional use of this invaluable tool. I am speaking of actions like Revenue Ruling 81-216 and the decision to halt future commitments to enter into tax-exempt loan guarantees that are used to provide access to necessary capital for firms that would otherwise be unable to gain access to or carry the cost of such financing.

These and other adverse rulings and actions continue in effect, despite congressional directives urging the restoration of these nec-

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essary forms of pollution control financing. As a result, economic expansion, so vital to the Nation's economic recovery, has been hampered because firms dependent upon this assistance to finance the mandatory, nonproductive costs of pollution control facilities have had their lifeline—that is, tax-exempt financing—abruptly severed.

I would now like to speak on the issue of the absence of any SBA commitments of guarantees for tax-exempt pollution control loan guarantees.

On December 31, 1981, the SBA announced its decision to no longer enter into loan guarantee commitments for tax-exempt pollution control loans. Despite congressional prodding on numerous occasions, the SBA has consistently refused to restore the availability of such guarantees for tax-exempts. This has placed many businesses closer to the edge of a financial precipice. Time does not allow for an indepth review of the importance of this program, but denial of pollution control loan guarantees for tax-exempt bonds will only exacerbate this already dire situation as firms attempt to expand and are unable to acquire capital to install pollution control facilities mandated by the Congress.

The SBA pollution control loan guarantee program has played a vital role in minimizing the discrimination small businesses have traditionally faced. Lenders view these concerns as higher risks and are, therefore, reluctant to provide them with capital to finance pollution control facilities. By making guarantees available to these firms, the SBA program has enhanced the financial attractiveness to lenders of making loans to small businesses, thereby enabling them to comply with environmental requirements.

There is another side to this program that deserves attention. This is the contribution the program makes to the budget on the revenue side. Since its inception, this SBA guarantee program has been a revenue raiser through the SBA fees levied on businesses using the guarantee. To date, the fee system has generated $25 million. Translated into program outputs, this means that the program is self-sustaining. It costs the Federal Government nothing and, more importantly, fosters economic activity throughout the country.

From the Council's perspective, taxable issue guarantees are an unrealistic alternative to the tax-exempt program. Small- and medium-sized businesses will find it difficult, if not impossible, to secure credit on taxable terms because they pose too great a risk to the lender. The debt service, also, in many cases, would represent too great a burden on those particular firms for this kind of investment.

I draw your attention to the response that SBA received following its retroactive policy change concerning the termination of the tax-exempt program. SBA notified over 100 businesses to either switch to the taxable guarantee route or face withdrawal of their applications. In response, one firm out of this total notified SBA of its desire to seek a taxable guarantee. And this is only for the principal of the loan. Clearly, the large majority of these companies believe, as I do, that the costs become prohibitive under the taxable guarantee option.

To the best of my knowledge, in Baltimore there are no firms that have sought the guarantee under the taxable option. There had been some firms that we were working with in connection with the tax-exempt guarantee option earlier.

It is unfortunate, but nonetheless clear, that the SBA and OMB have refused to heed the words of Congress and those in the industrial community that the provision of tax-exempt pollution loan guarantees is of vital importance to the survival of businesses. It is important to note that in many instances the company's net worth is exceeded by the costs of these pollution control facilities. So, as you can imagine, a business that does not have the assets to use as collateral for a taxable loan will have to close its doors or be in noncompliance with environmental mandates. These alternatives are unacceptable. As a result, the council strongly endorses the committee's decision to legislatively correct the unfortunate misunderstanding that has developed concerning the purpose of the SBA pollution control loan guarantee program.

Specifically, the council supports the committee's untiring efforts to secure the provision of tax-exempt pollution control loan guarantees through H.R. 6086. It is our understanding that sections 2, 3, and 6 of this bill would restore the SBA pollution control loan guarantee program to the status it held prior to December 31, 1981. As this committee is painfully aware, the authorization of this program has been subjected to constant turmoil and uncertainty over the past year. Congress authorized $250 million for loan guarantees in fiscal year 1982. However, the Office of Management and Budget determined unilaterally that only $50 million in such guarantees was necessary.

Soon after that decision, the Office of Management and Budget decided that $95 million would be necessary, but the issue of tax-exempts remained uncertain. Finally, OMB determined that $150 million would be allocated in fiscal year 1982, but the majority of the allocation would only be for taxable loans. These decisions have ultimately led to a complete halt in program activity because of the restrictions and uncertainty over program allocation.

It is obvious that the use of a ceiling in this program is unreliable. We hope that section 2 of H.R. 6086 that imposes a floor for such guarantee allocations will once and for all clarify the issue of how much authority will be available to enter into guarantee commitments to those whose economic activities are dependent upon a clear signal on the amount of assistance available, especially during these turbulent economic times.

Another paramount concern of the users of pollution control loan guarantees is the decision to preclude the SBA from entering into commitments for tax-exempt guarantees.

I will skip over some of this and say that it is certainly our hope that the committee maintain the intent of section 3 when it marks up H.R. 6086. Without such a legislative mandate, we will be back before the committee next year expounding upon the dilemma faced by businesses unable to find either affordable capital or access to capital because of their size.

Finally, section 6 of H.R. 6086 fills an important void in the continuing battle over precise data on the need for such loan guarantees. With the compilation of the users of such tax-exempt guaran-

tees, we will be in a better position to accurately gage the amount of such loan guarantee authority necessary each year.

I would like to just summarize the remainder of the testimony, which deals with the concern over the administration's proposals that generally affect the use of industrial revenue bonds. We recognize that there have been some instances of abuse of revenue bonds, that there may be some need to place some restrictions on the use of revenue bonds. In doing that, we would hope that the administration and Congress would recognize the importance of pollution control facilities as an eligible item for the use of tax-exempt financing.

We would also hope that the proposed requirement of a 1-percent commitment by local government would not find its way into any future legislation. We would also hope that Congress would recognize that in placing restrictions on the use of industrial revenue bonds that it is important that type of tool be targeted on the areas of greatest need. I am referring to distressed cities like Baltimore.

Let me conclude my remarks by reiterating that the Council of Pollution Control Agencies strongly supports the legislation that has been proposed, that we feel that this will greatly assist communities like Baltimore, where there are many small firms that need the tax-exempt guarantees through the SBA for pollution control equipment.

As I indicated earlier, on behalf of Baltimore, we are also supportive of many of the other features of the bill. With that, I will conclude my remarks and prepare to answer any questions.

[The prepared statement of Mr. Berkowitz follows:]

PREPARED STATEMENT OF BERNARD BERKOWITZ, PRESIDENT, BALTIMORE ECONOMIC DEVELOPMENT CORP., ON BEHALF OF THE COUNCIL OF POLLUTION CONTROL FINANCING AGENCIES

Mr. Chairman, members of the Committee, I am Bernard Berkowitz, President of the Baltimore Economic Development Corporation, and a member of the Council of Pollution Control Financing Agencies. The Council is a non-profit organization formed by state and local agencies which serve as issuers of tax-exempt financings for pollution control and solid waste facilities. The Council includes Associate Members from the financial, legal and industrial sectors. Council members have been active in supporting the continued availability of tax-exempt financing as an important part of the nation's effort to achieve environmental goals and foster a sustained economic recovery.

Before I turn to my prepared remarks concerning H.R. 6086 and the Council's views, I would like to take a moment and acknowledge the tremendous help that Baltimore City has received from you, Mr. Chairman, in the form of projects as well as legislative matters. Mayor Schaefer especially appreciates your invaluable assistance in the past. I personally value the friendship which we have had that goes back at least 15 years to the days when you headed the community action agency in Baltimore. Secondly, although I'm not here to testify on all of H.R. 6086, I do want you to know that we in Baltimore support all of the amendments you have proposed in H.R. 6086, especially those for the equal opportunity loan program and MES BIC's.

On behalf of the Council, I welcome this opportunity to provide the Committee with our views regarding H.R. 6086, and the overall dire circumstance surrounding the availability of tax-exempt pollution control financing. This Committee is to be commended for its continuing efforts to help navigate small business through these troubled economic waters. H.R. 6086 personifies this deep seated concern for small business, the largest source of new jobs and economic activity in the nation.

The Administration has proposed several changes to current tax policy it believes will reduce the growth in the volume of pollution control bonds. Additionally, during the past year, the Administration made preemptive administrative decisions that struck deep into the functional use of this invaluable tool. I am speaking of

actions like Revenue Ruling 81-216 and the decision to halt future commitments to enter into tax-exempt loan guarantees that are used to provide access to necessary capital for firms that would otherwise be unable to gain access or carry the cost of such financing. These and other adverse rulings and actions continue in effect, despite Congressional directives urging the restoration of these necessary forms of pollution control financing. As a result, economic expansion, so vital to the nation's economic recovery, has been hampered because firms dependent upon this assistance to finance the mandatory, nonproductive costs of pollution control facilities have had their life-line—tax-exempt financing—abruptly severed.

I would now like to speak on the issue of the absence of any SBA commitments of guarantees for tax-exempt pollution control loan guarantees.

On December 31, 1981, the SBA announced its decision to no longer enter into loan guarantee commitments for tax-exempt pollution control loans. Despite Congressional prodding on numerous occasions, the SBA has consistently refused to restore the availability of such guarantees for tax-exempts. This has placed many businesses closer to the edge of a financial precipice. Time does not allow for an in-depth review of the importance of this program so I have included examples of how beneficial tax-exempt pollution control financing is.

Denial of pollution control loan guarantees for tax-exempt bonds will only exacerbate this already dire situation as firms attempt to expand and are unable to acquire capital to install pollution control facilities mandated by the Congress.

The SBA Pollution Control Loan Guarantee program has played a vital role in minimizing the discrimination small businesses have traditionally faced. Lenders view these concerns as high risks and are therefore reluctant to provide them with capital to finance pollution control facilities. By making guarantees available to these firms, the SBA program has enhanced the financial attractiveness to lenders of making loans to small businesses, thereby enabling them to comply with environmental requirements.

There is another side to this program that deserves attention. This is the contribution the program makes to the budget on the revenue side. Since its inception, this SBA guarantee program has been a revenue raiser through the fee SBA levies on businesses using the program. To date, the fee system has generated $25 million. Translated into program outputs, this means that the program is self-sustaining. It costs the federal government nothing and, more importantly, fosters economic activity throughout the country.

From the Council's perspective, taxable issue guarantees are an unrealistic alternative to the tax-exempt program. Small and medium sized business will find it difficult, if not impossible, to secure credit on taxable terms because they pose too great a risk to the lender. As evidence of the lack of enthusiasm for the taxable guarantee alternative as a viable option, I draw your attention to the response SBA received following its retroactive policy change concerning the termination of the tax-exempt program. SBA notified over 100 businesses to either switch to the taxable guarantee route or face withdrawal of their applications. In response, one firm out of this total notified SBA of its desire to seek a taxable guarantee. And this is only for the principal of the loan. Clearly, the large majority of these companies believe, as I do, that the costs become prohibitive under the taxable guarantee option.

It is unfortunate, but nonetheless clear, that the SBA and OMB have refused to heed the words of Congress and those in the industrial community that the provision of tax-exempt pollution loan guarantees is of vital importance to the survival of businesses. It is important to note that in many instances the company's net worth is exceeded by the costs of these pollution control facilities. So, as you can imagine, a business that does not have the assets to use as collateral for a taxable loan will have to close its doors or be in non-compliance with environmental mandates. These alternatives are unacceptable. As a result the Council strongly endorses the Committee's decision to legislatively correct the unfortunate misunderstanding that has developed concerning the purpose of the SBA pollution control loan program.

Specifically, the Council supports the Committee's untiring efforts to secure the provision of tax-exempt pollution control guarantees through H.R. 6086. It is our understanding that Sections 2, 3, and 6 of this bill would restore the SBA pollution control loan guarantee program to the status it held prior to December 31, 1981. As this Committee is painfully aware, the authorization of this program has been subjected to constant turmoil and uncertainty over the past year. Congress authorized $250 million for loan guarantees in fiscal year 1982. However, OMB determined unilaterally that only $50 million in such guarantees was necessary. Soon after this decision, OMB decided that $95 million would be necessary, but the issue of tax-exempts remained uncertain. Finally, OMB determined that $150 million would be

allocated in fiscal year 1982, but the majority of the allocation would only be for taxable loans. These decisions have ultimately led to a complete halt in program activity, because of the restrictions and uncertainty over program allocation. It is obvious that the use of ceiling in this program is unreliable. We hope that Section 2 of H.R. 6086 that imposes a floor for such guarantee allocations will once and for all clarify the issue of how much authority will be available to enter into guarantee commitments to those whose economic activities are dependent upon a clear signal on the amount of assistance available—especially during these turbulent economic times.

Another paramount concern of the users of pollution control loan guarantees is the decision to preclude the SBA from entering into commitments for tax-exempt guarantees. As I stated earlier, the SBA alternative of taxable loan guarantees assists only those who do not require such a guarantee. It does nothing for firms who must resort to a government backed loan. It is therefore our strong hope that the Committee maintains the intent of Section 3 when it marks-up H.R. 6086. Without such a legislative mandate, we will be back before this Committee next year expounding upon the dilemma faced by businesses unable to find either affordable capital or access to capital because of their size. The Council stands ready to offer whatever assistance the Committee may need on this issue.

Finally, Section 6 of H.R. 6086 fills an important void in the continuing battle over precise data on the need for such loan guarantees. With the compilation of the users of such tax-exempt guarantees, we will be in a better position to accurately gauge the amount of such loan guarantee authority necessary each year.

I would like to take this opportunity to quickly review some of our concerns regarding the proposal to curtail the availability of tax-exempt financing for pollution control facilities.

Many in the Administration have argued that pollution control financing does not serve a public purpose. This was most recently articulated by Assistant Secretary of the Treasury John Chapoton, when he testified before this Committee's Subcommittee on Energy, Environment and Safety Issues Affecting Small Business. The Administration further posits, and I quote from its explanation of its tax proposal to restrict the use of Industrial Development Bonds:

". . . Businesses requiring pollution control facilities, through the use of tax-exempt financing creates a bias in favor of investment in those activities."

These views are especially troubling to us for it clouds the true intentions of recent proposals to restrict the availability of IDBs.

First, pollution control bonds do in fact serve a public purpose as currently used. These bonds enable businesses to finance the mandatory costs of non-productive pollution control equipment mandated in the Clean Water Act, Clean Air Act and the Resource Conservation and Recovery Act. I must add that these laws were just recently implemented (latter part of the 1970s) which I believe accounts for the recent use of pollution control bonds that has been the focus of much discussion.

Second, the Administration proposal to demand a one percent commitment is unrealistic. I know of only three states that have authority to enter into such commitments. This proposal is unworkable in the other states where localities are constitutionally prohibited from entering into such commitments. In an attempt to address the issue of bona fide uses of tax-exempt financing the Administration has taken a hatchet rather than a scapel to resolve its policy questions. The Council believes that any proposal to curtail IDB use should make a distinction between the use of IDBs for pure public purposes like clean air, water and land, and other IDB uses that do not readily serve an apparent public purpose.

Clearly, the public has spoken with regard to the value in pollution control equipment. In national polls, overwhelming majorities of Americans expressed a belief that the installation of pollution control equipment is necessary. More important, the public believes these pollution control expenditures and costs are desirable. With the proposals submitted by the Administration, the ability of business to finance the acquisition of such pollution control facilities is seriously jeopardized. The outcome of such proposals being implemented would mean the strong likelihood of a decreased environmental quality of life and increased business failures. In short, the Administration's proposals, I am afraid, would effectively abolish pollution control financing, despite overwhelming support for such environmental protection expenditures. With the passage of several pieces of legislation, Congress has set the agenda for a responsible policy of economic growth coupled with protection of our environmental heritage. The Congress has an obligation to provide us with the tools to meet these worthy objectives. Acceptance of the Administration proposals would be an abdication of this reponsibility and send the wrong signal to the American public on the priority of preserving our environmental resources.

This proposal is nothing short of an attempt to eliminate the use of tax-exempts. As the Administration pursues its "New Federalism," States and localities will be forced to assume the increased cost of financing additional services. Their ability to meet this one percent commitment is doubtful as deteriorating infrastructures demand commitment of scarce state and local resources. In effect, the Federal government is demanding we take on greater financial responsibilities while, at the same time, it seeks to remove the tools that are needed to accomplish these new duties. We welcome this reexamination of Federal-State-local responsibilities, but only so long as adequate tools are available to facilitate an orderly and effective restructuring of responsibilities over the long-term. Tax-exempt pollution control bonds, coupled with the availability of sufficient SBA authority to provide pollution control loan guarantees, is one such tool—and a critical one at that.

Mr. Chairman, this concludes my formal testimony. I would be pleased to respond to any questions the Committee may have at this time. Let me say once again that I appreciate you and your Committee's untiring efforts to pursue vigorously the implementation of this very important piece of legislation.

Mr. MITCHELL. Thank you very much. I don't have any questions. I merely wanted to reemphasize one point about the proposed 1-percent commitment on the part of a city to this program. Some of my colleagues have said to me, "Well, 1 percent isn't going to hurt anyone." I would simply point out that we are facing, in my city of Baltimore, the possible layoff of 1,000 public school teachers and employees simply because we can't raise another $12 million that is needed and, therefore, that 1 percent, though it may seem insignificant, assumes a great magnitude when you find a city as financially strapped as we are.

Thank you very much.

Mr. BERKOWITZ. May I say something about that?

Mr. MITCHELL. Yes.

Mr. BERKOWITZ. In calendar year 1980, in Baltimore there was nearly $200 million of revenue bond financing that was authorized, much of that for two large coal export port facilities. One percent of that amount would be $2 million. That is about 7 or 8 cents on the tax rate. The $2 million would pay for a lot of school teachers' salaries.

Mr. MITCHELL. It certainly would.

I am delighted that Congressman Daub has joined us. He will have to leave to attend the funeral of one of our colleagues. The funeral of Congressman John Ashbrook will be in Ohio, but I am very grateful that you could take a few minutes to be with us. Do you have questions?

Mr. DAUB. I do, Mr. Chairman. First, I would like to commend you sincerely for the hearing today and for an assembled list of appropriate testimony. Mr. Berkowitz, we welcome your expertise, not only because you have that expertise, but because you are a friend of the chairman and we are glad you are here this morning and some of your colleagues at home will be interested to know of your recorded testimony here, I am sure.

This committee voted unanimously, Mr. Chairman, in favor of continuing that guarantee on pollution control bonds, and I think it is an appropriate position for this committee to take, and I appreciate the very well-drafted testimony of the witness. Would you tell me, if you know, what the difference in cost would be between a typical tax-exempt pollution control loan guaranteed by SBA and one not tax exempt?

Mr. BERKOWITZ. It would be about a 3-percent spread.

Mr. DAUB. Are financial institutions willing to make non-tax-exempt loans under the pollution control guarantee program if businesses desire them, in your opinion?

Mr. BERKOWITZ. I think one of the problems for many of the small- and medium-sized firms is that when the financial institutions would take a look at the projections of income and expenses for the company and look at the debt service requirements, the additional debt service requirements, imposed by the additional interest spread and also by the probable decrease in the term of the loan, that the additional debt service burden in many cases would actually eliminate the ability of the company to even attain the non-tax-exempt form of financing.

Mr. DAUB. Can you estimate the number of businesses that now face the prospect of closing or severe curtailment, if they were unable to obtain that kind of a tax-exempt guarantee for a pollution control bond?

Mr. BERKOWITZ. I could not quantify that.

Mr. DAUB. Is there any way that could be quantified?

Is there any data on the drawing board that suggests there is a pent-up potential there that is just not being addressed?

Mr. BERKOWITZ. I think that with a great deal of difficulty the data could be quantified by looking at the firms and industries that will be required to pretreat their liquid wastes that have not yet complied with air quality control requirements and the size of those firms and their ability to undertake the improvements. Such a list could be put together with great difficulty.

Mr. DAUB. So, the nub of this is that because you don't add investment productive capacity, the lack of a guarantee makes what would normally be sufficient incentive—that is, the tax-exempt nature of the bond—not sufficient to proceed to capitalize out the mandated program.

Mr. BERKOWITZ. That is correct, Congressman Daub. You are adding to the expenses of the firm through increased debt service without increasing their income potential.

Mr. DAUB. Thank you very much, Mr. Chairman. I think that is important to have on the record.

Mr. MITCHELL. I agree. Thank you very, very much for being here, and I will be back in Baltimore sometime this evening.

Mr. BERKOWITZ. Thank you.

Mr. MITCHELL. Our next witness is Mr. Randal C. Teague, who is counsel for the Small Business Coalition for Pollution Control. Mr. Teague, thank you very much for taking time from what I know is a very busy schedule to be here.

TESTIMONY OF RANDAL C. TEAGUE, COUNSEL, SMALL BUSINESS COALITION FOR POLLUTION CONTROL

Mr. TEAGUE. Mr. Chairman, thank you very much. As you have indicated, I am Randal Teague and I am counsel to the Small Business Coalition for Pollution Control. I serve in this capacity as counsel to Vorys, Sater, Seymour & Pease, a Columbus, Ohio, law firm which is legal counsel to the coalition.

This coalition thanks you for giving it this opportunity to testify on an important matter affecting our economy. This committee is

to be congratulated by the small businesses of our country for the consistent leadership which this committee has shown on behalf of the Small Business Administration's pollution control facilities financing guarantee program. Its members are to be congratulated also for persuading their colleagues in the House of its continuing need and for making the case known time after time to an administration that is reining in sometimes excessive and unnecessary Federal loan and credit guarantee programs, but doesn't seem to know that this particular program is neither excessive nor unnecessary.

The Small Business Coalition was organized last year to heighten the awareness of Congress, the administration, and the public on the issues involved in determining the future of this SBA program. The coalition represents those small businesses which have, on the one hand, been required to install pollution control facilities and/or equipment in order to meet pollution control objectives of various levels of government and which, on the other hand, face either noncompliance with the statutes, regulations, plans, and orders reflecting those policies or a sale to a bigger business with more assets and borrowing leverage or insolvency and reorganization, if forced to overleverage or simply going out of business.

Our testimony today is directed at the Office of Management and Budget's and the Department of the Treasury's attacks on this particular SBA program. Those attacks are destroying this program. The consequences of these attacks include the undermining of other policy objectives of the administration, objectives with which this committee and this coalition would agree: Such as job creation, increased productivity, environmental protection, and tax revenue generation.

Mr. Chairman, what the administration has failed to recognize is that this is not a liberal versus conservative, or a majority versus minority, or a Democratic versus Republican issue. Liberal and Democratic-registered black businessmen, and conservative and Republican-registered businesswomen are being treated equally by the administration's policies in this regard. They are being treated very badly.

The discrimination here is on the basis of the common denominator which links existing and prospective applicants: The fact that they are small businesses. This is true because, while the administration has shut off tax-exempt pollution control financing for small businesses, big businesses still qualify under other administration policies, and remain wholly within the tax-exempt bond market today.

In the prepared testimony which I have submitted for the permanent record, I indicate in the State of Ohio, as an example, three large bond issues for pollution control in the month of March alone. This is one State in one month, and those include a $50 million Ohio Air Quality Development Authority bond guarantee for Ohio Edison Co., an $8.5 million water pollution control revenue bond issue for the General Motors Corp., and a $65 million pollution control revenue bond issue for Republic Steel. If you add those three together in one State, in one month, they are the equivalent of the entire SBA program for small business nationwide for pollution control for the entire fiscal year.

My complaint is obviously not at the State of Ohio or at the administration for permitting these pollution control objectives to be met. They are simply doing their job. My complaint is that big businesses are still involved in the program, while the administration has initiated and carried forward within the past year a policy which denies that participation to small business.

Congress should not permit this sad state of economic affairs to be continued by the administration and this is why we support legislative efforts to reverse that administration policy and its attacks on this program.

Briefly, why are both the Federal guarantee and the exemption from Federal income taxation necessary with respect to this program? Principally, for two reasons: First, extensive facility and equipment expenditures are, indeed, necessary to control air and water pollution and to manage solid waste disposal in order to comply with Federal, State, and local environmental policy objectives; and second, obtaining ordinary debt financing without the guarantee and tax-exemption is nearly impossible because of the disproportionate cost of the equipment in relation to most small businesses' net worth and profitability. Also, the equipment itself generally has little collateral value.

Yet, the administration continues to ignore these realities. The administration's most recent statements with respect to the SBA program and IDB's generally are contained in Assistant Secretary of the Treasury for Tax Policy John E. Chapoton's statement on March 31 to this committee's Subcommittee on Energy, Environment, and Safety Issues Affecting Small Business. In general, the Chapoton statement repeats the administration's major criticisms of industrial development bonds, that they crowd out of the market other tax-exempt issues for governmental purposes and that they create a substantial loss to the Treasury. It also adds some new twists to these arguments and in our written statement, we refute these arguments one by one and we call your attention and the administration's attention to that refutation.

Mr. MITCHELL. May I interrupt you for just a moment? On what page did you make those refutations?

Mr. TEAGUE. Mr. Chairman, the refutations begin on page 7 of the written statement.

Mr. Chairman, it seems to me that there is an arrogance in the assertions made by Treasury, which cannot go unmentioned. That arrogance arises from believing that because one has thought of impediments to existing policies that it is the first time that anyone has thought of those impediments. Yet, these impediments have been thought through by Congress and they have been rejected by Congress. They were fully considered by Congress in its 1975 and 1976 considerations of the legislation which led to the enactment of this SBA program. Those arguments were rejected in the constitutional processes of the formulation of this law, which processes this administration has sworn to uphold and defend.

Regrettably, the administration has been unwilling to recognize that it made a mistake in restricting the annual guarantee authority level in attaching a proviso to the reduced level, which prohibited the further use of the program authority for guaranteeing bonds exempt from Federal tax.

If it were a matter of opinion, the administration's initial decision and continued intransigence would be, at least, understandable. But it is not a matter of opinion. It is a matter of fact and on those facts the administration is clearly wrong. It has reached the wrong conclusions because it has relied on the wrong facts and on the wrong conceptual premises.

All the administration has had to do since December 31, 1981, is to recognize this, and then remove the proviso contained in OMB's December 31, 1981 rescheduling document, a removal which would require the scripting of only one sheet of paperwork in its transmittal from OMB to SBA. This would end this entire controversy, and without further dollar and other costs to the applicants, and their Representatives in Congress. This has not happened and if the March 31 testimony of Assistant Secretary Chapoton is any indication of the present administration attitude, which it certainly is, it isn't likely to happen.

Legislative remedies, therefore, appear to constitute the only viable course to pursue. The principal difficulty with the legislative course arises from the complexity of the public policies and statutes which govern, first, this SBA program; second, the tax exemption of industrial revenue bonds; and, third, OMB's authority to restrict the program no matter what Congress says about SBA authority and in Internal Revenue Code enactments and through the exercise of its powers under the Impoundment Control Act of 1974.

The coalition supports the legislation pending in Congress; in particular, your bill, Mr. Chairman, H.R. 6086, and the Conte-Bedell bill introduced yesterday to save this program. We believe that this legislation is compatible and can be meshed together into a very effective remedy.

Thank you.

[The prepared statement and attachments of Mr. Teague follow:]

PREPARED STATEMENT OF RANDAL C. TEAGUE, COUNSEL, SMALL BUSINESS COALITION FOR POLLUTION CONTROL

Mr. Chairman and Members of the Committee:

You are to be congratulated by the small businesses of our country for the leadership which you have shown on behalf of the Small Business Administration's pollution control facilities financing guarantee program. You are to be congratulated for persuading your colleagues of its continuing need and for making the case known, time after time, to an Administration that is reigning in excessive and unnecessary Federal loan and credit guarantees but doesn't seem to know that this particular program is neither excessive nor unnecessary. You and your capable Committee and Subcommittee staff are to be thanked particularly. It is not something the members of our Coalition will forget.

My testimony today is offered on behalf of this Coalition, The Small Business Coalition for Pollution Control. My testimony is directed at the Office of Management and Budget's (OMB) and Department of the Treasury's attacks on the Small Business Administration's (SBA) pollution control facilities industrial revenue bond financing guarantee program. Those attacks are

destroying this important program.

The real consequences of this attack include the undermining of other policy objectives of the Administration: jobs creation, increased productivity, environmental protection and tax revenue generation. As set forth in a recent letter from Ohio Governor James A. Rhodes to Chairman Bedell of your Subcomittee on Energy, Environment and Safety Issues Affecting Small Business, jobs are an important and desirable consequence of this program, some nearly 8,000 jobs in the state of Ohio alone. That letter is part of that Subcommittee's March 10 hearing record.

This is not a liberal vs. conservative issue, not a majority vs. minority issue and not a Democratic vs. Republican issue. Liberal and Democratic-registered black businessmen and conservative and Republican-registered white businesswomen are being treated equally by the Administration's policies: Badly. The discrimination here is on the basis of the common denominator which links existing and prospective applicants: The fact that they are small businesses. This is true because, while the Administration has shut off tax exempt pollution control financing for small businesses, big businesses still qualify under other Administration policies and remain in the tax exempt bond market today.

There are hundreds of examples of big businesses remaining in that market while small businesses have been excluded, but two have hit the president of our Coalition particularly hard for they involve his community of Dayton, Ohio. In March alone of

this year an Ohio Edison Company project was announced for $50,000,000 (see Appendix 1), a General Motors Corporation project was announced for $8,500,000 (see Appendix 2), and a Republic Steel project was announced for $65,000,000 (see Appendix 3). This was happening while the president of our Coalition was being told as a small businessman by the Administration in Washington that he and similarly situated pollution control facilities owners could no longer anticipate tax exemption for the bonds required to finance their facilities because that Administration had, for all intents and purposes, strangled the SBA program upon which he relied.

Congress should not permit this sad state of economic affairs to be continued by this Administration, and this is why we support legislative efforts to reverse that Administration policy and its attack on this program.

The Small Business Coalition for Pollution Control

I am Randal C. Teague, Counsel to The Small Business Coalition for Pollution Control. I serve in that capacity as a Counsel to Vorys, Sater, Seymour & Pease, a Columbus, Ohio law firm which is legal counsel to the Coalition.

The Coalition was organized last year to heighten the awareness of Congress, the Administration and the public of the issues involved in determining the future of the SBA's pollution control facilities and equipment financing guarantee program.

The Coalition represents those small businesses which have,

on the one hand, been required to install pollution control facilities and/or equipment in order to meet pollution control objectives of the Government and which, on the other hand, would face either (1) noncompliance with the statutes, regulations, plans and orders reflecting those policies, or (2) a sale to a bigger business with more assets and borrowing leverage, or (3) insolvency or reorganization, if forced to over-leverage, or (4) going out of business.

The president of the Coalition is Jack L. Schaefer, president of The Specialty Papers Company, a small business qualified specialty printing company in Dayton, Ohio.

On behalf of the Coalition, I would propose to discuss briefly: (1) the history of this program, (2) the need for its survival, (3) the Administration's actions toward the program, (4) the Administration's most recent statements concerning the program, and (5) a response to those statements which looks toward a legislative remedy.

History of the SBA Pollution Control Facilities Program

The Small Business Administration's pollution control facilities financing program is really a pollution control facilities and equipment financing program. It was authorized by sections 102-103 of the Small Business Investment Act of 1976 (P.L. 94-305, 90 Stat. 663, 15 U.S.C. 692, 13 C.F.R. 111) which amended the Small Business Investment Act of 1958 to allow small businesses to obtain access to the tax exempt bond markets for

the financing of plant changes and equipment mandated by pollution control regulation (air and water pollution control and solid waste management).

These statutes authorized SBA to guarantee up to one hundred percent of the payments due from eligible small businesses under qualified contracts for the planning, design, financing or installation of pollution control facilities and/or equipment.

The current limit on a loan guarantee is $5,000,000 principal plus interest, and the average is $1,200,000. The maximum term of the loan is 30 years; the average is 20 years. The applicant must demonstrate the need to overcome financing disadvantage in order to qualify. The applicant pays a guarantee fee of 3.5-percent times principal plus interest, less an escrow deposit of 3 monthly payments. In the event of default, payment is made from the escrow fund first, then from the fund created by the guarantee fees collected and the interest earned thereon. The $15 million revolving fund established by Congress at the beginning of the program has grown through the addition of these fees to over $30 million. It is our understanding that the few defaults experienced are being, or probably will be, recovered by SBA through subsequent agreements with the defaulting small businesses.

The Need

Why is this Federal Government guaranteed and tax-exempt financing necessary? Principally for two reasons:

1. Extensive facility and equipment expenditures are

necessary to control air and water pollution and manage solid waste disposal in order to comply with Federal, State and local environmental policy objectives; and

2. Obtaining ordinary debt financing without the guarantees and tax exemption is nearly impossible because of (a) the disproportionate cost of the equipment in relation to most small businesses' net worth and profitability and (b) the equipment itself generally has little collateral value.

This need has been reflected by the growth in applications received and loan principal guaranteed. This growth did not diminish during the past year's disruption of the program. In a capsule, the growth and the need that growth reflects has been as follows:.

Year	Companies Assisted	Principal	Aver. Prin./Co.
FY77	12	$ 5.7 million	$ 475,000
FY78	14	9.9 million	707,143
FY79	45	41.5 million	922,222
FY80	77	98.5 million	1,279,220
FY81	66	99.9 million	1,513,636

It must be stressed here that the number of applicants measured against the limited available authority assures that this program is indeed one of "last resort." SBA has $129 million of pollution control applications which have been received by it during the past 18 months. There are $35.6 million in commitments outstanding and $93.4 million awaiting processsing.

Administration Actions Toward The SBA Pollution Control Facilities Financing Guarantee Program

In brief, the OMB and Treasury have taken the following administrative actions toward the program:

1. Placed the annual authority ceiling at $150 million in FY82 and FY83 rather than the $250 million ceiling contemplated by existing enactments;

2. Provided that all FY83 authority be available only for taxable rather than tax-exempt bond issues; and

3. Limited SBA's ability to provide staffing for administration of the program.

These actions have essentially prevented small business from utilizing this approach to the financing of pollution control facilities and equipment.

The Administration's Position and the Coalition's Response

The Administration's most recent statements with respect to the SBA program and IDBs generally are contained in Assistant Secretary of the Treasury for Tax Policy John E. Chapoton's statement on March 31 to the Subcommittee on Energy, Environment and Safety of the House Committee on Small Business (see Appendix 4). I ask that Mr. Chapoton's prepared statement be appended to this testimony, as well as excerpts from the unedited transcript of the actual testimony (see Appendix 5).

In general, the Chapoton statement repeats the Administration's major criticisms of IDBs: That they "crowd out" of the market

other tax exempt issues for governmental purposes and that they create a substantial revenue loss to the Treasury. It also adds some new twists to these arguments and goes further than anyone in the Administration has to date in attempting to justify the inequities created by its policies. I propose to highlight portions of the statement and offer responses thereto.

"The volume of tax exempt pollution control obligations issued for private businesses was $3.8 billion in 1981, representing approximately 7 percent of the entire long term tax exempt market, and will be an estimated $4.2 billion in 1982."

Even at the $250 million level originally authorized, the SBA program is a tiny part of the total issuances of tax-exempt pollution control obligations. Some of the SBA guaranteed bonds are no doubt categorized as small-issue IDBs rather than pollution control bonds. When measured against the entire market for pollution control and other IDBs, the amount represented by SBA guaranteed bonds appears even more miniscule. This program is vital to the companies which seek to use it. Its "crowding out" effect is insignificant.

"The proliferation of tax exempt bonds has made them less cost-effective as subsidy mechanisms for private activities."

This statement translates to "interest rates are high." They have been for a prolonged period. The Administration does appear to recognize that demand for tax-exempt obligations is now reduced (while continuing to predict an increase in volume in 1982). In fact, the Public Securities Association reports that IDB volume was down 57% to $93 million when compared to January 1981 issuances. To the Coalition these factors indicate (1) that

the tax exempt bond market is correcting itself - clarification of the legislative status of IDBs will remove an artificial stimulus to IDB volume which has existed since early 1981; and (2) it is more difficult than ever for small businesses to obtain affordable pollution control financing - thus the survival of the SBA program is more important than ever to these businesses.

"...in our view the cost of controlling pollution should be regarded as part of the cost of producing goods and should be reflected in market prices."

Small businesses eligible for the program under discussion almost never have sufficient market share to enjoy price elasticity. Thus, the costs to a small business for controlling pollution often cannot be passed onto the consumer unless all businesses in the relevant market are required to achieve the same level of pollution reduction. That is seldom, if ever, the case either because of varying requirements or foreign competition. The fact is that those small businesses able to finance compliance with pollution laws will have to absorb those costs, which in turn will render them poorer credit risks in the first place. Thus the circle completes itself by causing those businesses to be less able to obtain conventional financing, or generate additional revenues from sales, which jeopardizes the small businesses' existence. The true cost of killing this program will be passed onto the taxpayer through lost jobs and lost tax revenue, together with higher prices for those products manufactured by surviving large businesses or imported from nations which do not impose the same pollution requirements.

"...providing tax exempt financing for investments in pollution control facilities ...results in a higher level of investment in polluting industries and a lower investment in other economic activities."

The naivete' of that statement is startling. The statement somehow assumes that polluting activities are restricted to a few businesses and are evidence of inherently evil activities. Nonsense! Virtually every human activity, including paperwork, generates waste which constitutes pollution if it is not adequately handled. Small businesses governed by pollution control laws run the gamut of agricultural and industrial activities. The business of the Coalition's president is being required to control solvents evaporating from inks used on printing presses. Hundreds of small Ohio electroplaters are being required to control discharges of acids, caustics and heavy metals resulting from activities ranging from creating printed electronic circuits to preventing corrosion on small parts found in innumerable types of machinery and vehicles. Small foundries, agricultural cooperatives, appliance manufacturers and metal fabricators, dry cleaning shops, food processors, chemical manufacturers and formulators, paint and coating manufacturers, paving contractors, and virtually every other product-oriented business within our economy can and does generate pollution which must be controlled. The Administration's position against "polluting industries" would seem to allow for few "clean" and approvable pursuits.

"...most pollution control bonds are issued to finance pollution control facilities

for new plants rather than existing plants. Thus, the 'transition rule' argument for tax exemption is no longer applicable in the majority of cases."

We don't have the statistics available to the government, but we believe that statement is patently untrue, at least as it affects small business. There are extensive new pollution control requirements which have not yet been met by existing small businesses throughout the nation. In our cities, wastewater pretreatment requirements and volatile organic compound emission requirements are only now taking effect. The next round of tighter permit requirements under the National Pollution Discharge Elimination System are about to be issued. And the pollution control facilities of the 1970's have often created, because of collection and concentration, a new pollutant of the 1980's - hazardous waste. In many instances businesses previously in compliance with air pollution laws will now also have to control sources of fugitive emissions because ambient air quality standards have still not been met. The compliance problems facing existing small businesses because of current pollution control requirements are still formidable. The argument that the problem of financing pollution control facilities is now confined largely to new plants seems to us to be made up out of whole cloth.

"Placing the credit of the United States behind an obligation that is exempt from Federal taxation creates a security which is superior in the market to the direct obligations issued by the Federal government. A Federally guaranteed tax exempt obligation also has a distinct competitive advantage over all other tax exempt obligations issued by State and local governments."

Once again, the SBA program is very small. The Government competes with those bonds through its indirect obligations, especially those of government corporations, e.g., the Tennessee Valley Authority or the Bonneville Power Administration, whose obligations are guaranteed and the income from which is tax-exempt. Does anyone suspect that anything other than the faith and credit of the United States stands ultimately behind TVA, Bonneville and similar bonds? These obligations are a much larger factor in the bond market than the SBA guaranteed bonds.

"...the Public Debt Act of 1941 prohibits the Federal government from issuing tax exempt obligations directly..."

We find it disturbing that the spirit of a 1941 Act is given precedence over the letter of the subsequent Small Business Investment Act of 1976 (Public Law 94-305) and over the legislative history of the Joint Resolution making further continuing appropriations for the fiscal year 1982 (Public Law 97-92). Apparently, Treasury ignores the relevant canons of legislative construction to which its policy would be held in a court of law, to wit: (1) That the letter of the law takes precedence over its spirit and (2) that, when there is conflict between legislative enactments (or legislative intents), the most recent in time takes precedence.

One has a feeling that the Public Debt Act of 1941 was found after the fact in order to justify the OMB decision. It was not an impediment, with the Department of the Treasury or anywhere else, to the first five years of this program. The legislative history of the 1941 Act is clear that the guiding principle

behind the enactment of the prohibition on tax exemption of these 1941 Act obligations was the realization that these obligations produced no tax revenues to offset the tax losses which would occur from tax exemption. That is, these U.S. Government obligations had no offsetting tax revenue gains. The SBA guaranteed bonds, on the other hand, do have offsetting tax revenue gains. They are in the form of Federal corporate taxes paid by the small businesses and Federal individual income taxes paid by their officers and employees, some 250 businesses and 20,000 employees in the history of the program to date. Each time a small business obtains tax exempt financing and remains in business thereby, revenues are increased in the best case circumstances and maintained in the worst case circumstances. Conversely, the absence of the SBA program would create a high risk of tax revenue losses arising from those businesses closing down and laying off their employees.

There is an arrogance in a way in the assertions made by Treasury which cannot go unmentioned. It must arise from believing that because one has thought of impediments to existing policies that it is the first time anyone has thought of them. These "impediments" have been thought through and by Congress; they have also been rejected. They were fully considered by Congress in its 1975 and 1976 consideration of the legislation which led to the enactment of this SBA program, and those arguments were rejected in the constitutional processes of the formulation of this law, which processes this Administration has

sworn to uphold and defend. I draw your particular attention to the text of the House (then Select) Committee on Small Business' 1975 hearings, "SBA Assistance for Agricultural Concerns and to Meet Pollution Control Problems," and the subsequent reports (H. Rpts. 94-519 and 94-115) as support for these observations.

The Ultimate Administration Fallacy:
The New, Taxable Bonds Will Still Be "Tax Exempt"

The taxable bonds which OMB and Treasury would have guaranteed by a modified pollution control facilities financing program will still escape current Federal taxation because they will be purchased, if at all, by pension funds.

There is within our economy no existing market for Federally-guaranteed taxable pollution control bonds. There is no market because such an obligation has not yet existed. In order for such Federally-guaranteed taxable bonds to be marketed, a market will have to be created for them. That can be done. It is a matter of determining the characteristics of these bonds and then the most likely purchasers of them.

The Coalition has surveyed the investment banking community associated with the program as it existed prior to OMB's and Treasury's attacks upon it. There are several possible markets, but there is agreement that the most probable market for Federally-guaranteed taxable bonds is pension funds. It is that reality which defeats OMB's and Treasury's intentions in prohibiting SBA from guaranteeing tax-exempt bonds, for pension funds are exempt from Federal income taxation. Thus, they will

be paid a higher rate of interest by the small businesses, but they will not have to pay taxes currently on that higher rate.

The SBA guaranteed loan program for tax-exempt financing of pollution control facilities is a matter of survival for many small businesses. It is essential to participants in the program and insignificant in the Treasury. It should be permitted to continue within the framework of the existing law.

Towards a Legislative Remedy

The deepest regret within this entire controversy has been the unwillingness of the Administration to recognize that it made a mistake in restricting the annual guarantee authority level and in attaching a proviso to the reduced level which proviso prohibited the further use of the program authority for guaranteeing bonds exempt from Federal tax. If it were a matter of opinion, the Administration's initial decision and continued intransigence would be at least understandable. But it is not a matter of opinion; it is a matter of facts. And on those facts, the Adminstration is clearly wrong. It has reached the wrong conclusions because it has relied on the wrong factual and conceptual premises. All the Administration has had to do since December 31, 1981 is to recognize this and then remove the proviso contained in OMB's December 31, 1981 rescheduling document, a removal which would require the scripting of only one sheet of paperwork and its transmittal from OMB to SBA. That would end this entire controversy and without further dollar and

other costs to the applicants and their Representatives in Congress. But this has not happened, and if the March 31 testimony of Assistant Secretary Chapoton and his April 23 letter on the tax exemption of industrial revenue bonds (see Appendix 6) are any indications of present Administration attitude, as they must be, it is unlikely to happen.

Legislative remedies, therefore, appear to constitute the only viable course to pursue. The principal difficulty with the legislative course arises from the complexity of the public policies and statutes which govern, first, this SBA program; second, the tax exemption of industrial revenue bonds; and, third, OMB's authority to restrict the program no matter what Congress says in its SBA authority and Internal Revenue Code enactments.

The Coalition supports the legislation pending before this Committee, particularly H.R. 6086 by Mr. Mitchell. While the specific language differs in these two bills, we believe they are compatible. We have prepared and attached as Appendix 7 to this statement two proposed amendments to H.R. 6086, amendments designed to go the extra measure required to restrict OMB's ability, even if this legislation becomes law, to circumvent it again. The amendments are offered as friendly amendments for the Chairman's and this Committee's considerations. It is our opinion that this legislation, if amended, would prevent OMB from frustrating this program again far more effectively than any language now on the statute books.

Unfortunately, Congress could still unravel this important program by amendments to the Internal Revenue Code of 1954 too severely restricting the availability of tax exemption for the industrial revenue bonds on which these SBA applicants rely. The preservation of the small issue exemption frustrated by Revenue Ruling 81-216 is crucial; Congress must reinstitute that small issue exemption. Let me be more specific.

Under present law, the small business required to install pollution control equipment has two alternatives in pursuing tax-exempt financing. First, it can seek to qualify its facilities under Section 103(b)(4) of the Internal Revenue Code as an "exempt facility". Under existing Treasury Regulations, however, this approach requires an analysis of financiable costs which is one of the most complex engineering and legal tasks with which I am familiar. This process typically adds thousands of dollars to the cost of issuance of bonds to finance pollution control facilities. The second alternative available to small businesses is the small issue IDB exemption under Section 103(b)(6) of the Internal Revenue Code. These issues can be qualified for tax-exempt financing within the $1 million or $10 million limitations without resort to the difficult and detailed tax analysis to which larger pollution control issues are subjected. The fact that qualifying "exempt facilities" financing is unlimited as to dollar amount is, as a practical matter, irrelevant to small business. Such businesses lack borrowing capacity in excess of the $1 million to $10 million range. Thus, even if exempt

facilities financing is retained, the elimination or constriction of the small issue exemption would severely hamper the ability of small business to finance pollution control facilties.

Certain of the Administration's proposals to make changes in IDB legislation would effectively put an end to the ability of small business to obtain affordable financing for pollution control facilities. For example, the requirements that the local government make a contribution or financial commitment to the financed facility creates an obvious problem. Even if state law were to permit such contribution, I doubt that many local communities would allocate limited resources toward the financing of pollution control facilities for small business as opposed to competing for location in the community of new facilities, particularly those of substantial size perceived to offer much greater potential benefits to the community.

We implore the Members of this Committee to work with their colleagues on the House Committee on Ways and Means and Senators from their States or otherwise on the Senate Committee on Finance to assure the continuation of tax exempted industrial revenue bonds for pollution control purposes, including preservation of the pre-Rev. Rul. 81-216 small issue exemption.

Unfortunately, that done, the Administration could, even in the face of two additional Congressional enactments (an SBA omnibus bill and a 1982 tax reform bill) by that time, frustrate the Congressional intents reflected in those enactments by exercising its authority to restrict Federal loan and credit

guarantees. OMB knows that its authority to so restrict is not limited by the Impoundment Control Act of 1974 because Federal loan and credit guarantees are not within the definition of a budget item which either requires OMB to report such an "impoundment" to Congress or gives Congress standing in the courts if OMB persists in the face of Congressional directives to the contrary. It is our opinion that Congress will not have tied OMB's hands in this matter beyond any reasonable doubt until the Impoundment Control Act of 1974 is amended to include Federal loan and credit guarantees within the relevant definition of what constitutes an actionable impoundment.

The foregoing notwithstanding, your Committee is engaged in the winning of a significant battle in this particular war, and the Coalition and its members commend you for it.

Summary

The Coalition believes that Congress should direct Treasury and all other entities involved in the administration of tax policy, e.g., OMB, to carry out the intent of existing legislation with respect to the SBA Pollution Control Facilities Financing Guarantee Program. The program is vital for the small businesses which can participate. We believe it preserves and may enhance the collection of tax revenues.

The case for this position is clear. The merits of this program are:

- The program actually makes money for the U.S. Government.
- The program does not make a measurable impact on the operation of the capital markets.
- The program does permit access by small business to those capital markets.
- The program constituted less than 1% of the small IRB issues in FY81 and will be less than 1% in FY82.
- The program has demonstrable public benefits, particularly the abatement and control of pollution.
- The program has one of the smallest administrative staffs on record.
- The program is funded with private sector funds, guaranteed by the Federal Government.

We urge your favorable consideration of the recommendations set forth herein.

OFFICIAL STATEMENT

$50,000,000

Ohio Air Quality Development Authority

State of Ohio

11¼% AIR QUALITY FACILITIES REVENUE BONDS,

1982 Series A (Ohio Edison Company Project)

Due October 1, 1992

The Bonds will be special obligations of the State of Ohio, issued by the Ohio Air Quality Development Authority on behalf of the State of Ohio to provide funds for air pollution control facilities and will be payable from revenues of the Authority derived from the pledge of payments to be made on an Air Quality Facilities Note delivered to the Trustee by Ohio Edison Company and from funds drawn under an Irrevocable Letter of Credit issued by

Bankers Trust Company

The Letter of Credit will permit the Trustee to draw up to an amount equal to principal of and seven months' interest accrued on the Bonds on or prior to the stated maturity thereof.

Principal and semi-annual interest (April 1 and October 1, commencing October 1, 1982) are payable at the principal corporate trust office of Society National Bank, Cleveland, Ohio, Trustee, and Bankers Trust Company, New York, New York, Co-Paying Agent. The Bonds, which are dated April 1, 1982, are issuable in coupon form in the denomination of $5,000 each, registrable as to principal only, and as fully registered Bonds in the denomination of $5,000 or any multiple thereof. Coupon Bonds and fully registered Bonds are interchangeable. The Bonds are subject to redemption prior to maturity as more fully described herein.

PRICE 100% AND ACCRUED INTEREST

In the opinion of Ballard, Spahr, Andrews & Ingersoll, Bond Counsel, interest on the Bonds is exempt from Federal income tax as enacted and construed on the date of issuance except as provided in Section 103(b) (10) of the Internal Revenue Code as to any such Bonds held by a substantial user of the Project Facilities or by a "related person", as such term is defined in Section 103(b) (6) (C) of the Code; and under the laws of the State of Ohio as enacted and construed on the date of issuance, the interest on the Bonds is exempt from Ohio personal income tax and Ohio municipal income taxes, and, so long as exempt from Federal income tax, from Ohio corporate franchise tax, and the Bonds are exempt from Ohio intangible property taxes.

The Bonds are offered, subject to prior sale, when, as and if issued by the Authority and accepted by the Underwriters and subject to the approval of legality by Bond Counsel, and approval of certain legal matters by Simpson Thacher & Bartlett, counsel for the Underwriters, and certain other matters. It is expected that delivery of the Bonds will be made on or about April 14, 1982 at the office of Morgan Stanley & Co. Incorporated, 55 Water Street, New York, New York, against payment therefor in New York Clearing House funds.

MORGAN STANLEY & CO.
Incorporated

E. F. HUTTON & COMPANY INC.

SHEARSON/AMERICAN EXPRESS INC.

March 31, 1982

OFFICIAL STATEMENT

Ohio Water Development Authority
$8,500,000
State of Ohio
9¼% Pollution Control Revenue Bonds, 1982 Series A
(General Motors Corporation Project)

The 1982 Series A Bonds, to be issued to provide funds for pollution control facilities, will be special obligations of the State of Ohio issued by the Ohio Water Development Authority and will not constitute a debt, or a pledge of the faith and credit, of the Authority or the State or of any political subdivision thereof, and the holders or owners of the 1982 Series A Bonds will have no right to have taxes levied by the General Assembly of the State or the taxing authority of any political subdivision of the State for the payment of the principal thereof or interest or any premium thereon. The 1982 Series A Bonds will be payable solely, except to the extent paid out of moneys attributable to proceeds of the 1982 Series A Bonds, from and secured by a pledge and assignment of moneys to be derived from a Loan Agreement with

General Motors Corporation

Dated March 1, 1982 **Due as shown below**

Holders of 1982 Series A Bonds will have the right to elect to have their 1982 Series A Bonds redeemed by the Authority on March 1, 1985 at 100% of the principal amount thereof plus accrued interest. Such election must be made by delivering such 1982 Series A Bonds to Citibank, N.A., New York, New York, as Escrow Agent, on or before 4:00 P.M. New York time on November 30, 1984 but not before November 1, 1984 and may be withdrawn not later than January 31, 1985. The Company will have the option to purchase on March 1, 1985 all but not less than all 1982 Series A Bonds for which such redemption election has been made and not withdrawn. The Company may hold, resell, deliver to the Trustee under the Indenture for cancellation or otherwise dispose of 1982 Series A Bonds so purchased. If a holder of a 1982 Series A Bond elects to have 1982 Series A Bonds redeemed on March 1, 1985 and does not withdraw such election, the Company has the unconditional obligation to provide funds which will be used to purchase or redeem such 1982 Series A Bonds at par plus accrued interest on March 1, 1985. The Company may, but will be under no obligation to, make an offer to have any or all of such holders electing to redeem at such time withdraw their redemption elections. Thus, the Company could, but would be under no obligation to, agree to purchase the 1982 Series A Bonds at later dates on such terms and conditions, which could vary among particular electing holders, as may be agreed upon between the Company and the particular electing holders.

The 1982 Series A Bonds will be issuable as coupon bonds in the denomination of $5,000 each, registrable as to principal only, and as fully registered bonds in the denomination of $5,000 or any integral multiple thereof. Coupon 1982 Series A Bonds and fully registered 1982 Series A Bonds will be interchangeable. Principal and semi-annual interest (March 1 and September 1, first payment September 1, 1982) will be payable on coupon 1982 Series A Bonds at the principal corporate trust office of AmeriTrust Company, Cleveland, Ohio, the Trustee and paying agent. The 1982 Series A Bonds will be subject to mandatory and optional redemption as more fully described herein.

9¼% 1982 Series A Bonds due March 1, 2012—Price 100%
(plus accrued interest)

In the opinion of Bond Counsel, under existing law, interest on the 1982 Series A Bonds, except on any 1982 Series A Bond for any period during which it is held by a "substantial user" of the Project or a "related person" as those terms are used in Section 103(b)(10) of the Internal Revenue Code of 1954, is exempt from Federal income tax. The 1982 Series A Bonds will be exempt from Ohio taxes to the extent described herein under "Tax Exemption."

The 1982 Series A Bonds will be offered when, as and if issued by the Authority and accepted by the Underwriter and subject to the approval of legality by Squire, Sanders & Dempsey, Cleveland, Ohio, Bond Counsel, and certain other conditions. It is expected that the 1982 Series A Bonds in definitive form will be available for delivery on April 21, 1982.

The First Boston Corporation

The date of this Official Statement is March 26, 1982.

OFFICIAL STATEMENT

$65,000,000
State of Ohio
Pollution Control Revenue Bonds
(Republic Steel Project)

The Bonds, issued to provide funds for air quality facilities, will be special obligations of the State of Ohio issued by the Ohio Air Quality Development Authority and, except to the extent payable from Bond proceeds and the investment thereof, will be payable solely from loan payments to be made by Republic Steel Corporation and funds drawn under an irrevocable Letter of Credit issued by

Morgan Guaranty Trust Company of New York

The Letter of Credit will permit AmeriTrust Company, Cleveland, Ohio, as Trustee, to draw up to $65,000,000 to pay the principal of the Bonds, up to $4,280,209 to pay seven months of interest and up to $1,950,000 to pay any redemption premium on the Bonds. The portion of the Letter of Credit to be used to pay interest on the Bonds will be automatically reinstated after each drawing unless the Trustee has received notice that an event of default has occurred, in which case the principal of and premium, if any, and interest on the Bonds will be declared immediately due and payable by the Trustee and the Trustee will draw on the Letter of Credit to pay the Bonds. The Letter of Credit expires April 16, 1992. If Republic Steel Corporation fails to arrange for the extension of the Letter of Credit upon expiration, it has the right to deliver to the Trustee a substitute letter of credit, provided that such substitute letter of credit results in the Bonds being rated no lower than their initial ratings or the ratings which the Bonds would then have if the Letter of Credit were extended, whichever are lower. If the Letter of Credit is not extended and Republic Steel Corporation does not arrange a substitute letter of credit, the Bonds will be redeemed at redemption prices more fully described herein. Prior to the expiration of the Letter of Credit on April 16, 1992 and upon occurrence of certain events as more fully described herein, Republic Steel Corporation may replace the Letter of Credit with a substitute letter of credit of another bank.

Dated April 1, 1982 **Due April 1, 2012**

$25,000,000 9¾% Series L Bonds — Price 100%
$40,000,000 12¼% Series M Bonds — Price 100%
(plus accrued interest)

Holders of the Series L Bonds and the Series M Bonds will have the right to demand redemption of their Bonds on April 1, 1985 and April 1, 1992, respectively, and to receive payment for their Bonds to be redeemed at 100% of the principal amount thereof plus accrued and unpaid interest to the redemption date. In the case of Series L Bonds, such redemption election must be made by delivering Series L Bonds to be redeemed to Society National Bank, Cleveland, Ohio, as Escrow Agent, between November 15, 1984 and December 14, 1984 and may be withdrawn no later than March 1, 1985. In the case of Series M Bonds, such redemption election must be made by delivering Series M Bonds to be redeemed to the Escrow Agent between November 15, 1991 and December 13, 1991 and may be withdrawn no later than February 28, 1992.

The Company has the right to purchase all Bonds for which redemption elections have been made and not withdrawn. The Company may hold, resell, retire or otherwise dispose of Bonds so purchased. Prior to the expiration of the withdrawal period described above, the Company may make offers to have Bondholders electing to be redeemed at such time withdraw their redemption elections, including offers by the Company to purchase Bonds at a later date or dates.

Principal and semiannual interest (April 1 and October 1, commencing October 1, 1982) will be payable at the principal corporate trust office of the Trustee. Coupon Bonds in the denomination of $5,000 each, registrable as to principal only, and fully registered Bonds of the same series without coupons in denominations of $5,000 or any integral multiple thereof, will be exchangeable at the principal corporate trust office of the Trustee. The Bonds will be subject to redemption as more fully described herein.

In the opinion of Bricker & Eckler, Bond Counsel, under existing law, interest on the Bonds, except on any Bond for any period during which it is held by a "substantial user" of the Project or a "related person", as those terms are used in Section 103(b)(10) of the Internal Revenue Code of 1954, as amended, is exempt from federal income taxes, and is exempt from the Ohio personal income tax and municipal income taxes in Ohio and, so long as exempt from federal income taxes, from the Ohio corporate franchise tax, and the Bonds are exempt from Ohio intangible property taxes.

The Bonds will be offered when, as and if issued by the Authority and received by the Underwriters and subject to the approval of legality by Bricker & Eckler, Columbus, Ohio, Bond Counsel, and certain other conditions. It is expected that the Bonds in definitive form will be available for delivery in New York, New York on or about April 8, 1982.

The First Boston Corporation — Merrill Lynch White Weld Capital Markets Group
Merrill Lynch, Pierce, Fenner & Smith Incorporated

The date of this Official Statement is March 31, 1982.

[Appendix 4]

For Release Upon Delivery
Expected at 9:00 a.m. EST
March 31, 1982

STATEMENT OF
THE HONORABLE JOHN E. CHAPOTON
ASSISTANT SECRETARY (TAX POLICY)
DEPARTMENT OF THE TREASURY
BEFORE THE
SUBCOMMITTEE ON ENERGY, ENVIRONMENT AND SAFETY
OF THE
HOUSE SMALL BUSINESS COMMITTEE

Mr. Chairman and Members of the Subcommittee:

I am here today to discuss the views of the Treasury Department on guarantees by the Small Business Administration (SBA) of tax exempt industrial development bonds issued to finance pollution control facilities.

The Treasury Department opposes SBA guarantees of tax exempt pollution control obligations. In addition, the Administration is now proposing that Congress enact additional restrictions on all types of private purpose tax exempt bonds. Before commenting upon our particular concerns with respect to pollution control obligations and the SBA program, I would like to review some of the factors that have caused us to conclude that additional limits are needed on all types of private purpose tax exempt bonds.

There has been a virtual explosion in the last five or six years in the issuance of private purpose tax exempt obligations. This includes bonds issued for single family housing, student loans, and nonprofit hospitals and colleges as well as industrial development bonds (IDBs). More than $25 billion were issued in 1981, up from $8.5 billion in 1976. Private purpose bonds accounted for 24 percent of the long term tax exempt bond market in 1976, but rose to 48 percent in 1981. The Treasury Department estimates that 55 percent of the tax exempt bonds sold in 1982 will be for private activities. The volume of tax exempt pollution control obligations issued for private businesses was $3.8 billion in 1981, representing approximately 7 percent of the entire long term tax exempt market, and will be an estimated $4.2 billion in 1982.

The largest growth has occurred in small issue IDBs, which allow virtually any business to obtain tax exempt financing for land or depreciable property. Small issue IDBs have been used extensively by the largest corporations in the country. For example, one of the largest retailing chains has used small issue IDBs to finance $240 million of facilities since 1976. Small issue IDBs marketed in 1981 were an estimated $10.5 billion of the total $25 billion of private purpose bonds. Small issues represented 20 percent of the entire long term tax exempt market in 1981, as compared with only 4 percent in 1976. The estimated revenue loss to the Federal Treasury from small issue IDBs alone will be $1.65 billion in fiscal 1982 and will exceed $2.1 billion in fiscal 1983 unless additional restrictions are imposed. Moreover, we estimate that less than 15 percent of the new investments made in 1981 that were eligible for small issue IDB financing were in fact financed by that method. This means that the potential for future growth in the volume of small issue IDBs remains enormous.

The proliferation of private purpose tax exempt bonds -- along with reduced demand for tax exempt bonds by institutional investors and the tax rate reductions and other structural tax changes enacted in the Economic Recovery Tax Act -- has contributed to a significant narrowing of the difference in interest rates between tax exempt and taxable bonds. While the tax exempt rate historically has been about 65 to 75 percent of the taxable rate, issuers of tax exempt bonds currently have to pay about 80 to 85 percent of the taxable rate. This erosion of the relative advantage of tax exempt financing has increased significantly the interest costs incurred by state and local governments in financing essential public services and facilities.

The increasing volume of private purpose tax exempt bonds has also caused mounting Federal revenue losses. We estimate that the total Federal revenue loss from private purpose tax exempt bonds outstanding in fiscal year 1981 was $3.22 billion and will be $4.19 billion for fiscal 1982.

The proliferation of tax exempt bonds has made them less cost-effective as subsidy mechanisms for private activities. Tax exempt financing has often been criticized as an inefficient means of granting Federal subsidies. The revenue loss to the Treasury from the income tax exemption is significantly greater than the interest cost savings to users of the bond proceeds. For example, if we assume that an investor in the 40 percent bracket purchases a bond bearing interest at 70 percent of the taxable rate, the Treasury loses $1.33 for every $1.00 of interest savings to the bond user. Even more of the benefit is siphoned off by investors as tax exempt bond rates grow closer to taxable rates, as they have recently.

These and other considerations have caused us to conclude that additional restrictions are needed to reduce the growth of private purpose tax exempt obligations. The specific details of our proposal are described in the general and technical explanations released by the Treasury Department on February 26. Copies of those explanations are attached to this statement.

The special provision for small business under our proposal relating to small issue IDBs should be of particular interest to this Subcommittee. Under the Administration's proposal, small issue IDBs will be retained for businesses that have capital expenditures of less than $20 million over the 6-year period from 3 years before to 3 years after the issuance of the bonds. In addition, no single firm will be able to have over $10 million of IDB-financed facilities at any one time. However, subject to these restrictions, small issue IDBs could be marketed as a part of a composite or umbrella bond issue. These changes will make it easier for small and medium-sized businesses to use small issue IDBs and will prevent the use of small issue IDBs by large corporations that are able to raise funds readily in capital markets without an interest subsidy from the Federal government.

I would now like to discuss the policy considerations relating specifically to tax exempt financing for pollution control facilities and the SBA guarantee program.

It is often argued that Federal assistance for construction of pollution control facilities is justified because pollution control requirements are special burdens imposed on businesses by government. However, in our view the cost of controlling pollution should be regarded as part of the cost of producing goods and should be reflected in market prices. The consumption of goods produced by techniques that create air or water pollution as a by-product will be excessive if the market prices of those goods do not reflect all production costs. Thus, providing tax exempt financing for investments in pollution control facilities produces undesirable economic distortions, in that it results in a higher level of investment in polluting industries and a lower level of investment in other economic activities. Another result of the subsidy is that part of the cost of controlling pollution is borne by taxpayers in general, rather than by the purchasers of the goods produced.

Tax exempt financing for pollution control facilities also has been justified in the past by the need to assist businesses in bringing existing plants into compliance with new pollution control requirements. Now, however, most pollution control bonds are issued to finance pollution control facilities for new plants rather than existing plants. Thus, the "transition rule" argument for the tax exemption is no longer applicable in the majority of cases. Furthermore, it is difficult in many cases to determine what portion of a newly constructed plant constitutes pollution control facilities, particularly if the plant employs new or innovative processes or equipment rather than facilities of a type that have previously been recognized as qualifying for tax exempt financing. This inevitably creates an undesirable bias against new technology and in favor of particular types of pollution control equipment which are recognized as eligible for tax exempt financing.

Providing Federal guarantees for tax exempt obligations raises additional problems. Placing the credit of the United States behind an obligation that is exempt from Federal taxation creates a security which is superior in the market to the direct obligations issued by the Federal government. A Federally guaranteed tax exempt obligation also has a distinct competitive advantage over all other tax exempt obligations issued by State and local governments. As a result, Federal guarantees of tax exempt obligations increase the borrowing costs of Federal, State and local governments. Because of these and other considerations, the Treasury Department has consistently opposed Federal guarantees of tax exempt obligations. Moreover, the Public Debt Act of 1941 prohibits the Federal government from issuing tax exempt obligations directly; and numerous other statutes preclude Federal guarantees of tax exempts in other contexts. Allowing SBA guarantees of tax exempt pollution control obligations would be directly contrary to the policies expressed by Congress in those enactments.

Finally, in these times of budgetary constraint, we believe that SBA guarantees of tax exempt obligations would represent an unwarranted duplication of Federal benefits. Both the SBA guarantee and the income tax exemption are implicit subsidies that reduce the interest rate that borrowers must pay. In view of the pressures on the tax exempt bond market and the inherent inefficiencies involved with using tax exempt financing as a subsidy mechanism, we believe that it is appropriate for the Small Business Administration to restrict its guarantee program to taxable financings.

I will be happy to answer your questions.

[APPENDIX 5]

UNEDITED EXCERPTS FROM MARCH 31, 1982 HEARING OF THE SUBCOMMITTEE ON ENERGY, ENVIRONMENT AND SAFETY ISSUES AFFECTING SMALL BUSINESS

MR. BEDELL. Mr. Chapoton, it's very clear. Either we are discriminating against small business or we're not.

If we have a ruling which says a big business, which needs $10 million worth of pollution control bonds, can sell those tax exempt bonds, but small businesses which need $50,000 worth of pollution control equipment, which is a bigger investment compared to their net worth than the $10 million to the big corporation, cannot get such financing, then, at least, I think almost everybody would say that if that's because of government rules and regulations, the government is discriminating against small business.

Now, the question is what the people that are making these rules believe. And I guess the first question is, do the people that are making these rules believe that is is not discriminating against small business for this tax exempt financing in practical use to be unavailable to small business where it is available to big business because of the rulings of those people in Treasury and in policies of the Treasury and OMB?

It's very clear. Either it's available to both or it's not available to one. And if it is not available to one, why is it not available? At least some of us think it's because of your rulings. And if that is the case, then the question is, is your ruling because you don't understand that small business cannot, in effect, sell, for practical purposes, a $50,000 20-year pollution control bond?

And if you think they can, then we need to get your thinking straight because you've testified that you don't want to discriminate.

MR. CHAPOTON. If discrimination exists, it is not because of Treasury or OMB rulings. There are problems for small business that don't exist for large business. But in small business --

MR. BEDELL. Just a minute. I have to interrupt.

MR. CHAPOTON. Okay.

MR. BEDELL. Did your ruling or did your ruling not, in practicality, make it impossible for that company that needed $50,000 worth of pollution control equipment to get tax exempt financing for that equipment?

MR. CHAPOTON. It did not.

MR. BEDELL. Well if it did, would you then consider changing the ruling?

MR. CHAPOTON. No, I think the --

MR. BEDELL. You wouldn't change it even if it did?

MR. CHAPOTON. If it denies it, it's not because the ruling denied it. It's because the small business has a different problem.

MR. BEDELL. No, Mr. Chapoton, they could get it before. Before your ruling, they could get it. After your ruling, they cannot get it. Now, tell me, if that's the case, how your ruling had nothing to do with them not being able to get it?

* * * *

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MR. BEDELL. The other question the chairman would have is that you say, "Current law, however, does not require the showing of any genuine public purpose for the project to be financed with tax exempt obligations."

MR. CHAPOTON. That is correct.

MR. BEDELL. So you don't think that financing for pollution control equipment in and of itself shows public purpose?

MR. CHAPOTON. In many instances, when you look at the actual facts, it is very difficult to define public purpose.

MR. BEDELL. For the project to be financed?

MR. CHAPOTON. That's correct.

MR. BEDELL. You don't think they need to put in their pollution control --

MR. CHAPOTON. Oh, sure they need to put in pollution control to start up the plant.

MR. BEDELL. "Current law, however, does not require the showing of any genuine public purpose for the project to be financed with tax exempt obligations." These projects are pollution control projects. You do not think that pollution control projects necessarily serve a public purpose?

MR. CHAPOTON. As I stated earlier, indeed, financing it is probably not as -- financing at cheaper rates or subsidy is probably not a good public policy.

MR. BEDELL. No, but that's not what you said. "Current law, however, does not require the showing of any genuine public purpose for the project to be financed with tax exempt obligations." Public purpose for the project -- I took it that's what you meant or didn't you mean to say that?

MR. CHAPOTON. No, I meant to say that. There is no showing at a local level of a public purpose. The only showing is that for tax exempt financing to exist, that it be a nonproductive pollution control facility.

MR. BEDELL. Well, I hope that the record will clearly show that the Treasury Department thinks that there is no showing -- necessarily a public purpose for a project for pollution control equipment. I hope that this will clearly show that that's your testimony, because I'm pretty sure that they would want to know that in some of the other committees of the Congress, that you see no public purpose for projects to control pollution.

* * * * *

MR. ECKART. The small business person is going to have the EPA on one side of them, lack of financing capability on the other side of them, and they are going to opt to close their door. Closing their door as a direct result of two government activities -- one which tells them to do something and one which takes away from them their way out of answering what they are told to do.

And that is simply the only conclusion that I can draw from your testimony today, and the testimony that preceded you from small business people all around

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the United States. They want to comply with the Law. They want to meet what I believe to be a valid public purpose stated in the law, of controlling certain environmental emissions. And the only way out, because of their size and because of the cost and the complexity of installing the required equipment to meet the government needs, is being taken away from them.

So, therefore, this administration is holding their feet to the fire by its polcies and pouring gasoline on the fire at the same time. And I don't know where the small business person goes under those circumstances.

MR. CHAPOTON. Mr. Eckart, what you're assuming is once the EPA requirement is imposed upon the business, small or large, but in this case small business, that there should be a federal benefit, federal subsidy to help them meet that obligation. We make two points. One is that if you are going to do it, that tax exempt financing is very ineffecient way to do it, and perhaps I should emphasize that a lot more.

It is clearly an inefficient way to do it, and that a lot of the benefit goes to persons other than the user. That is, it goes to the tax exempt bond holder. In addition, the combined -- and really, the problem that is before the subcommittee today more than the ineffeciency of tax exempt financing, but the combined benefit of tax exempt financing and federal guarantee is a dual benefit and is inconsistent with a long standing federal credit policy of the government, not just this administration but of the government for a number of years.

It is not--it does--I understand the chairman's point that it denies access of small business to the long-term market, but I submit that that is the market place that denies that, not any policy.

Indeed, if we are going to cut out -- if we are going to erradicate that discrimination, that is, small business has less access to capital markets than big business, then we have to put a bias to small business and that is what the SBA program does. And in doing so, we conclude that it is inconsistent and undesirable and inefficient federal credit policy, and therefore, we do not want to continue it.

MR. ECKART. Well, if I make two assumptions-- number one, the assumption that it is, in fact, inefficient is true and I make a second assumption that you really don't think that there is, in fact, not a valid public purpose to controlling these pollution emissions, then what would be an efficient way of helping small business persons meeting --

MR. CHAPOTON. A much more efficient way would be a direct subsidy to small business to reduce their costs. Certainly all the benefit would then go to the small business, and it would be an on-budget type item.

MR. ECKART. Are you testifying in support of us increasing or making a direct appropriation in that regard?

MR. CHAPOTON. No, I'm not doing that but I am saying that if this money is to be spent that is now being spent through tax exempt financing for all pollution control, if it were done through a direct subsidy, it would be more efficient to the users.

MR. ECKART. But you're not supporting that?

MR. CHAPOTON. No, I'm not supporting that...

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[Appendix 6]

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

ASSISTANT SECRETARY

April 23, 1982

Dear Mr. Teague:

Thank you for your letter concerning private purpose tax-exempt bonds. I apologize for the delay in responding to your comments.

The use by state and local governments of their tax-exempt borrowing privilege for private activities has increased dramatically in recent years. More than $25 billion of tax-exempt bonds were issued for private activities in 1981, up from $8.5 billion in 1976. Private purpose bonds accounted for 24 percent of the entire tax-exempt bond market in 1976, but rose to 48 percent in 1981 and will consume an estimated 55 percent of the market in 1982. The estimated Federal revenue loss from private purpose tax-exempt bonds outstanding in fiscal year 1981 was $3.22 billion and will be $4.19 billion for fiscal year 1982.

The largest growth has occurred in "small issue" industrial development bonds (IDBs), which allow virtually any business to obtain tax-exempt financing for land or depreciable property. Small issue IDBs have been used extensively by many of the largest corporations in the country--firms that are able to raise funds readily in capital markets without an interest subsidy from the Federal Government. Approximately $10.5 billion of small issue IDBs were marketed in 1981, representing 20 percent of the entire long term tax-exempt bond market. The estimated Federal revenue loss from small issue IDBs alone will be $1.65 billion in fiscal year 1982 and will exceed $2.1 billion in fiscal year 1983 unless additional restrictions are imposed.

The proliferation of private purpose tax-exempt obligations has contributed to the significant narrowing of the difference in interest rates between tax-exempt and taxable bonds. While the tax-exempt rate historically has been about 65 to 75 percent of the taxable rate, tax-exempt bonds are now yielding approximately 80 to 85 percent of the taxable rate. This reduction in the interest savings from the tax exemption has increased the borrowing costs incurred by state and local governments in financing essential public

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services. It also has made tax-exempt financing less efficient as a subsidy for private activities. Tax-exempt financing has often been criticized as an inefficient subsidy because the Federal revenue loss from the income tax exemption exceeds the interest cost savings to the bond users. This problem is exacerbated as tax-exempt rates grow closer to taxable rates and a greater portion of the benefit is siphoned off for the bond investors.

It is argued that tax-exempt financing is a valuable tool that can be used by state and local governments to encourage the location of job-producing businesses in their communities. This argument may have had some merit in the past, when IDB financing was available in a limited number of localities. Now, however, IDB financing is available in almost every locality and offers no relative incentive to induce new business location in a particular community.

Federal law presently requires no effort to demonstrate that a local public purpose is to be served as a prerequisite to tax-exempt financing for a private activity. Indeed, some issuing authorities reportedly have authorized tax-exempt bonds for facilities located outside of their own boundaries. State and local governments and bond authorities in many cases have acted as mere conduits to provide entry into the tax-exempt market for activities that would not merit direct governmental assistance at either the Federal or local level.

It is also appropriate to reevaluate the benefits provided by IDBs in view of the additional tax incentives for new capital investment provided by the Economic Recovery Tax Act. The Accelerated Cost Recovery System (ACRS) and the investment tax credit produce tax savings that are generally sufficient to offset the future income tax liabilities attributable to investments in new equipment. When IDB financing is added, however, the combined benefits not only offset the future tax on income attributable to the equipment, but also reduce the tax on income from other investments. This may cause a firm to make investments in equipment that would be economically unprofitable.

The Administration's legislative proposal, which generally applies to bonds issued in 1983 and thereafter responds directly to the considerations outlined above. The tax exemption for private purpose bonds will be limited to those bonds that are publicly approved by local governments and which, for bonds issued after 1985, receive a financial

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contribution or commitment from the local government. Assets financed with tax-exempt bonds must be depreciated using the straight-line method over extended recovery periods. Small issue IDBs will not be allowed for large businesses. Subject to these restrictions, multiple lots of small issue IDBs could be sold as a part of a composite or umbrella bond issue. Additional requirements relating to information reporting, registration and arbitrage profits will be imposed. These additional limits should promote more prudent use of the Federal interest subsidy and help preserve the benefits of the program for those activities that are deemed to be the most deserving.

Thanks again for your interest in this matter.

Sincerely,

John E. Chapoton
Assistant Secretary
Tax Policy)

Mr. Randal Teague
Small Business Coalition for
Pollution Control
1828 L Street, N. W.
Washington, D. C. 20036

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(APPENDIX 7)

PROPOSED AMENDMENTS TO H.R. 6086, BY MR. MITCHELL:

1. On pages 2 and 3 thereof, beginning at page 2, line 18, and continuing through page 3, line 4, insert the language set forth herebelow in italicized print, as follows:

"(12) Notwithstanding any other provision of law, *rule, regulation or fiscal policy to the contrary,* the Administration shall enter into commitments to guarantee loans, debentures, payments of rentals or other amounts due under qualified contracts and other types of financial assistance and to enter commitments to guarantee sureties against loss pursuant to programs under this Act and the Small Business Investment Act of 1958 in the full amounts provided by law subject only to (A) the availability of qualified applications for such guarantees and (B) limitations contained in *the expressed language of* appropriation Acts. Nothing in this paragraph authorizes the Administration to reduce or limit its authority to enter commitments for such guarantees to qualified applicants.".

2. On page 3, strike lines 5 through 13 inclusively, and add in lieu thereof the following new language:

"Sec. 3. (a) Paragraph (1) of section 404(b) of the Small Business Investment Act of 1958 (relating to pollution control) is amended to read as follows:

"(1) Notwithstanding any other provision of law, rule, regulation or fiscal policy to the contrary, in the case of pollution control facilities or property with respect to which a guarantee is authorized, the determination of whether such a guarantee is issued shall be made without regard to whether such facilities or property are acquired by the use of proceeds from industrial revenue bonds the interest on which

is exempt from Federal income tax, and, subject only to the existence of qualified guarantee applications of eligible small business concerns and within the authority available to the Administration, the Administration shall not decline to issue the guarantee authorized in the case of such pollution control facilities or property which are acquired by the use of proceeds from said industrial revenue bonds the interest on which is exempt from Federal income tax."

(b) The amendment made by subsection (a) of this section shall apply to applications (for the issuance of a guarantee described in such amendment)

(1) pending on January 1, 1982, or

(2) made after December 31, 1981.

Mr. MITCHELL. Thank you very much for your very excellent testimony. I really don't have any questions. I have one comment.

It seems to me that the administration is defeating one of its major thrusts, that is, to control inflation, if it does not permit small businesses to use tax-exempt financing, because it is a cost.

Mr. TEAGUE. That is absolutely correct.

Mr. MITCHELL. It is a major cost to control pollution, and most of the small businesses that I know are not going to be able to absorb that cost out of any reserves that they have. They are going to pass that cost on and that, it seems to me, contributes to the very thing that the administration is determined to control, and that is further inflation.

Mr. TEAGUE. I think you are right there, Mr. Chairman.

In response to one of the previous questions, which was addressed to the previous witness, in our discussions with the 128 applicants that now have applications pending before SBA, I think there are several things which can be said. One is that no one is going to proceed. I confirmed this with the SBA yesterday in preparing my oral comments for this statement. The pollution control financing section within SBA has not closed on a single taxable issue since this proviso was mandated by the Office of Management and Budget.

In our discussions with the applicants, it is unlikely that they will proceed in requesting SBA to close on a taxable issue. Since we have been involved in this program over the last year, if you simply turn to the Wall Street Journal on a daily basis and look at the bond issues that are reported, you would see that the point spread between taxable and nontaxable issues has ranged from roughly 300 basis points to one period in early March of almost 575 basis points.

Our law firm represents commercial banks, S. & L.'s, and a host of financial institutions. We have met with these clients in an

effort to help the other clients and it is unlikely that any of these financial institutions would finance pollution control facilities and equipment for a longer period than 5 years. For the economics to work for most of these small businesses, they need 20 and 25 and in some cases even 30-year financing. They simply cannot absorb the additional cost within a 5-year period. If they did, they would have to pass that on in terms of higher price and that, quite frankly, would put them out of the market and then they would be out of business.

Mr. MITCHELL. Thank you very much. I am very pleased that Congressman McDade has joined us, the ranking minority member on the committee. Do you have questions?

Mr. MCDADE. Thank you, Mr. Chairman.

Mr. MITCHELL. How did you get free from Appropriations?

Mr. MCDADE. I am going there very shortly.

It is a pleasure to be with you, Mr. Chairman, and to hear the witness testify this morning. Let me ask you the same question that we asked the last witness. How many businesses actually face closures because of the current situation with respect to whether or not pollution bonds should be tax exempt or not?

Mr. TEAGUE. Well, let me talk in terms of the actual applications that are pending. At the time that the program was put in abeyance, there were roughly 130 applications pending; from the work which we have done, there are at least 6 or 7 of those which we can simply not find, and we think they have, in fact, closed their doors. That is not a particularly high percentage, but when you consider the fact that it is 6 or 7 that would be there today had the program not been put in abeyance, then it is, indeed, regretful.

My suspicion is that the real crunch, however, Congressman, will not come until the end of this year. In our work with the various Federal and State air and water quality administrations, most of them have been, quite frankly, a little bit more relaxed about the enforcement with respect to these small business applicants because they know that this matter is pending before Congress.

We had a meeting in Ohio several weeks ago, and the air and water people there told us that they would wait until the end of the session. If Congress did, in fact, act and the administration acquiesced in the congressional action and the program went forward, everybody's problem would be taken care of. But they are telling the small businesses in Ohio, at least, that if Congress does, in fact, not act this year or if Congress does act and the administration still continues to restrict the program under the Impoundment Control Act exemptions, then they simply at that point will be required by their own internal politics within the State to begin tightening up.

At that point, they would then begin enforcing the air and water pollution control requirements which the businesses cannot comply with and it is at that period that you would really begin to see the closing of the businesses or their sales to larger businesses that would have the leverage to be able to finance it within a 5-year period.

Mr. MCDADE. That is all I have. Thank you, Mr. Chairman.

Mr. MITCHELL. Thank you. In your response you present us with another catch-22 situation. If, because of the uncertainty of what

will happen in the Congress, States are not enforcing, then we are doing one of the things that the organization is bitterly opposed to. We are adding to the pollution problem.

Mr. TEAGUE. That is absolutely correct, Mr. Chairman.

Mr. MITCHELL. It seems to me imperative that we act in a very expeditious and forthright manner to get some legislation through.

Mr. TEAGUE. If this legislation is passed, you not only accomplish the pollution control objectives and the small business objectives, but you also accomplish the jobs creation objectives of Congress and also provide for tax revenue generation. The thing that is puzzling to me about the static estimates that are done by the Department of the Treasury with respect to the revenue projections on the so-called losses to the Treasury as a result of this program is that they do not put on the other side of the equation the losses in the corporate tax revenues and the losses in personal tax revenues occasioned by these small businesses going out of business if the program does not continue.

Mr. MITCHELL. Thank you for very, very cogent testimony.

Mr. TEAGUE. Thank you, Mr. Chairman.

Mr. MITCHELL. We will next hear from a panel: Mr. John Sower, representing the National Association of Development Companies and the National Development Council, Mr. Don Albertson, who is with the Iowa Business Growth Co., Mr. Vincent J. Matteo, Greater Scranton Chamber of Commerce, and Mr. Larry Smith, the Baltimore Economic Development Corp.

Gentlemen, thank you very much for being here. I appreciate your taking the time.

PANEL CONSISTING OF JOHN SOWER, LARRY SMITH, VINCENT J. MATTEO, AND DON J. ALBERTSON

TESTIMONY OF JOHN SOWER, WASHINGTON DIRECTOR, NATIONAL DEVELOPMENT COUNCIL, AND INCORPORATING PRESIDENT, NATIONAL ASSOCIATION OF DEVELOPMENT COMPANIES

Mr. SOWER. Thank you, Congressman. I will start. I am John Sower and I am the Washington director of the National Development Council and the incorporating president of NADCO, the National Association of Development Companies.

I will make a very short statement and submit a more complete statement for the record.

Mr. MITCHELL. Without objection, it will be submitted in its entirety.

Mr. SOWER. Thank you, Mr. Chairman.

I would like to introduce my three colleagues who are members of NADCO and represent certified development corporations, who will each speak from their perspective.

NADCO is a professional trade association of section 503 certified development companies and, like the program, it is fairly new. At this time the NADCO members represent CDCs which have completed approximately 55 percent of the loan volume in the program and about 58 percent of the dollar volume. Our first national membership meeting is here in Washington in June.

As you know, the 503 program provides long-term fixed-asset financing for smaller businesses and it is the SBA's primary econom-

ic development program. It creates jobs and is based on a local group of 25 people, usually Government officials, private sector individuals, and others working together in their community to help smaller business create jobs and expand.

It is based on the 502 program, which was a predecessor program, which, as you know, Congressman, was used for projects in Baltimore, such as Garwin Medical Center, Syndarm Plastics, Old Town Mall, and others.

We all know that the recession is deepening now, and that unemployment is increasing. Furthermore, we have all read the statistics that small businesses are the primary sources of new jobs in the economy. For that reason the 503 program should be a major focus of the administration in creating jobs and expanding private sector small businesses. It offers long-term financing for growth and expansion, and it fills the need for long-term financing that smaller businesses are not able to find. The National Association of Development Companies strongly urges that the Congress maintain the program's budget levels for fiscal year 1982 and 1983.

There are a couple of procedural issues that I wanted to review with you just briefly. First is that it is very difficult for 503's to be organized on a statewide basis at the present time and as Governors become more involved in economic development, this is something that needs to be reconsidered. A second procedural issue is that SBA's alter ego regulations make it difficult for smaller businesses to take advantage of the new tax act incentives of the Reagan administration and still qualify for SBA financing under this program.

Mr. MITCHELL. Do you want to clarify alter ego?

Mr. SOWER. Perhaps I could do that at a later time, Congressman. It is a long, technical matter.

Mr. MITCHELL. I know what you are talking about, and we can address it later.

Mr. SOWER. Thank you.

Another minor point is that SBA's regulations and operating procedures don't permit enough flexibility for fast-growing smaller businesses on the issue of expansion space. And a last point has to do with involvement of the 503 program with tax-exempt issues. Even though the conference report and the regulations permitted the 503 debentures to be subordinate to tax-exempt issues, the SBA's standard operating procedures have not permitted this. I don't know whether this is legal or not, but it certainly is prejudicial to smaller businesses and it is not consistent with what is the national need to create jobs in smaller businesses.

The last point is that the 503 program could use some airing out with some private sector involvement on some of these issues, consistent with the Reagan administration's efforts to stimulate private sector investment in the economy.

I will conclude at this point and I would like to start with Mr. Larry Smith, who is the senior vice president from the Baltimore Economic Development Corp. Next, we have Mr. Vincent Matteo, who is from Metroaction in Scranton, Pa. and last, Mr. Don Albertson, who is executive vice president of Iowa Business Growth Corp. in Des Moines, Iowa.

[The prepared statement and attachment of Mr. Sower follows:]

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PREPARED STATEMENT OF JOHN SOWER, WASHINGTON DIRECTOR, NATIONAL DEVELOPMENT COUNCIL, AND INCORPORATING PRESIDENT, NATIONAL ASSOCIATION OF DEVELOPMENT COMPANIES

PREFACE

INTRODUCTION

Good morning. My name is John Sower, and I am the Incorporating President of the National Association of Development Companies, which is called NADCO

I would like to make a very short statement, submit a more complete written statement for the record, and then ask three NADCO members to testify. They are:

Mr. Larry Smith
Senior Vice President
Baltimore Economic Development Corp. (BEDCO)
Baltimore, Maryland

Mr. Don J. Albertson
Executive Vice President
Iowa Business Growth Corp.
Des Moines, Iowa

Mr. Vince Mateo
Project Manager
Metro Action, Inc.
Greater Scranton Chamber of Commerce
Scranton, Pennsylvania

NADCO

NADCO is the professional trade association of the SBA Section 503 Certified Development Companies. It is a fairly new group and most of the larger and more active Section 503 CDCs are members. As of April 15, the NADCO membership was responsible for 55% of the loans approved under the 503 Program, which represents 58% of total dollar volume.

Our first annual membership meeting will be here in Washington on June 10 and 11. Many of the Section 503 CDCs will be in town for that meeting and they will be hoping to meet with members of Congress and committee staff to discuss the 503 Program.

We had a preliminary membership meeting in December of 1981 with Congressional representatives and SBA officials and that resulted in many helpful changes in the 503 Program.

FUNDING LEVELS

We all know that the recession is deepening and that unemployment is rising. Furthermore, we have all read the statistics that small businesses are the primary creators of new jobs in the economy. For that reason, the 503 Program should be a major focus of the United States government to create jobs in smaller business. It offers long-term financing for growth and expansion of viable growing businesses. It fills the need for long-term financing that all growing smaller businesses have if they want to expand and create new jobs. The National Association of Development Companies strongly urges that the Congress maintain the Program's budget levels for fiscal years 1982 and 1983.

PROGRAM ADMINISTRATION

Many NADCO members have contacted us regarding their problems with the increasing administrative complexities of the 503 Program. There are many minor technical points that could be fairly easily clarified and streamlined and that would improve the operations of the Program. For example:

1. Statewide 503s - present regulations make it almost impossible to organize a Section 503 CDC statewide, although Governors are assuming an increasingly important role in local economic development.

2. Tax Incentives - SBA's "alter ego" regulations make it very difficult for smaller businesses to take advantage of the Reagan Administration's Economic Recovery Tax Act incentives and still qualify for SBA financing.

3. Expansion Space - SBA's regulations are too restrictive for expanding, growing companies that need additional space.

4. Involvement with Tax Exempt Issues - both the conference report of the Congress and the regulations specifically permit Section 503 debentures to be subordinate to tax exempt obligations; yet SBA's operating procedures have prohibited this. This is probably illegal, is prejudicial against smaller business, and is certainly inconsistent with the nation's highest domestic needs to create jobs in growing smaller businesses.

Our members feel that the administration of the 503 Program needs a private sector "airing out" consistent with the Reagan Administration's efforts to stimulate private sector growth and investment in the economy. Perhaps some sort of advisory panel consisting of private sector representatives or SBA personnel with actual field experience could be established to help streamline and de-bureaucratize the program.

My complete written statement on the rationale for the 503 Program and its importance in the economy at this time has been submitted. I will now turn to the representatives of NADCO's member Section 503 CDCs to testify.

GROWTH CAPITAL FOR SMALLER BUSINESS

A NATIONAL ECONOMIC REVITALIZATION STRATEGY

SBA'S NEW 503 PROGRAM

I. THE ISSUES

A. Introduction

Our topic today is SBA's new Section 503 Certified Development Company Program — an important new tool to help smaller businesses increase their capital investment and thereby make a dent in the federal budget deficit by both paying more taxes and creating jobs which reduce unemployment payments.

This presentation will cover "why" the 503 program was created and "why" it is important.

I wear two hats as I speak today — first as Washington Director of the National Development Council, a private, nonprofit organization sometimes known as "economic development investment bankers." Over the past four years, we have helped 75 local communities to organize and implement their economic development financing programs creating $3.0 billion of capital investment in 3,000 small and medium-sized businesses and creating over 130,000 permanent, private sector jobs.

We have revolutionized the local economic development financing business by incorprating rigorous private sector management techniques and a network of financially skilled loan packagers in the nation's major cities. We have helped to institute "hard" policies of providing long-term, fixed asset financing for growing, healthy businesses to create permanent jobs rather than the "soft" money-losing policies of providing stop-gap aids to failing, marginal firms or high-risk start-ups.

My second hat is as unpaid Incorporating President of NADCO — the National Association of Development Companies — a new professional trade association representing the 172 Section 503 Certified Development Companies in local communities across the country.

B. The Economy

1. Introduction

We all know the state of the economy — we are officially in a recession. The tax reductions are just starting and more spending cutbacks are coming. Nonetheless, the pressures of both inflation and interest rates continue. Officials are now talking about an annual federal deficit for Fiscal Year '82 of nearly $100 billion.

2. Overlooked Small Business — Britain

We can learn some lessons about our own economy from the recent experience in Britain. The March 22, 1981 issue of the Miami Herald reported on a study of Britain's economy by Professor Allen Meltzer of Carnegie Mellon University, and states, "The most disturbing of Meltzer's findings about Britain is the failure of Thatcher's tax cuts to produce a spurt of investment."[1]

I'm no great student of the English economy but I am not surprised, as the large percent of their economy consists of government owned monopolies or large corporations supported directly or indirectly by the national government that don't pay much taxes — thus would not be much affected by the change in the tax rate. It is as if we had nationalized and then subsidized W. T. Grants, Chrysler, Amtrak and every other major corporation that has had problems — plus a hundred more.

The October 3rd issue of the Economist had a section on the American economy entitled "Oh, For a Burst of Growth." It stated, "A dash of growth, of course, would work wonders for the President's arithmetic, by cutting outlays and increasing tax revenues."[2] The same issue had a long article about the dynamic growth of smaller business in the English economy in the past decade — despite the adverse economic conditions in that country.

Interestingly, that issue of Economist missed the point — like a trout fisherman who doesn't see the fish swimming at his feet. An important source of new growth and investment in both their economy and ours is smaller business. Even through aggregate economic statistics show a recession with high unemployment and declining industries such as automobiles and steel, many smaller business sectors are booming — particularly those in the newer technologies such as electronics, energy, medicine and computers. Smaller businesses are rapidly creating new jobs, developing new technologies and generating tax revenues in hard-pressed communities.

Thus, a logical policy conclusion would seem to be to aggressively stimulate the growth and investment of smaller businesses, i.e., support your winners instead of your losers. We ought to be aggressively helping expanding, successful smaller business. Unfortunately, smaller business has not made it in terms of hard policy — certainly not in England nor in our own country.

3. Tax Cuts and Small Business

Tax cuts and tax credits help all businesses, as some of the small business groups have pointed out, they really don't stimulate as much capital formation for smaller businesses which are in lower tax brackets and are less capital intensive. Moreover, tax cuts do not help new businesses nor provide the steady infusion of new capital that is needed in all growing businesses — both large and small.

Tom Richmond, Washington Editor of Inc. magazine, stated in an October 1981 editorial entitled "Why Small Business Lost on the Tax Bill,"

"If...you take the position that a healthy economy, while necessary, is not by itself sufficient to insure accelerated growth in a declining small business sector — then small business didn't fare very well."[3]

David Stockman is reputed to have said, "I've never believed that just cutting taxes alone will cause output and employment to expand."[4]

I disagree. I think the President is right — but that it is just a matter of time — although unfortunately, it may take quite a bit of time.

As evidence, I suggest we look at the venture capital industry. A recent Business Week article stated, "After a veritable drought in venture capital investing before the 1978 capital gains tax cut to 28% from 49%, a near flood of money is rapidly reshaping the field. This year, the pool of funds used to back new inventions, technologies and companies is swelling to $6 billion from $2.8 billion in 1977."[5]

In summary — tax cuts will spur investment — gradually not explosively. In the meantime we need to accelerate the capital formation process in the fast booming smaller business area with policies and programs that provide growth capital for smaller businesses — such as SBA's Section 503 CDC program.

4. Need for Investment

We are all waiting for the "supply-side surge," the slow-in-coming increase in capital investment by the private sector that will generate empoyment, reduce unemployment payments and increase tax revenues — thus reducing the federal deficit and stimulating the nation's economic growth. However, we also need something more — we need more growth capital for smaller businesses — so that they can move now and lead the way out of this recession.

Growth capital is important in other countries as well — and it is more than just tax cuts. A recent British study on capital formation stated, "There is much evidence to indicate that the much envied economic performances, particularly in West Germany and Japan, are based primarily on the availability of long-term, low cost investment credit to their industries."[6]

The important issue, thus, is to find ways to stimulate more investment capital for the growing sectors of our economy — by different methods including tax cuts, reduction of regulations, lower interest rates and more growth capital, particularly for smaller businesses.

C. Importance of Small Business

1. Creation of Jobs

a. The role of small business in creating new jobs in the economy is increasingly realized. In 1979, David Birch of MIT wrote a report entitled "The Job Generation Process" emphasizing the importance of small business in creating new jobs. One conclusion was that "small firms (those with 20 or fewer

employees) generate 66% of all new jobs generated in the U.S."[7]

b. President Reagan, in his April 29, 1981 presentation to the Congress, stated, "Let us not overlook the fact that the small, independent business man or woman creates more than 80% of all new jobs and employs more than half our work-force."

c. George Gilder, one of the Administration's economic advisers, stated in a chapter entitled "The Entrepreneurial Future" in his book Wealth and Povery that "It is small and high technology businesses...that generate most of the employment in America....In addition, small firms provide more than 80% of the jobs for young blacks and other disadvantaged citizens."[8]

2. Technology and Innovation

Small businesses' contribution to innovation and technology development are also increasingly understood. The April 1980 report of the White House Commission on Small Business stated, "Small business has demonstrated incomparable innovative fertility. The National Science Foundation study disclosed that, for every R&D dollar, small companies produce four times more innovation than medium-sized companies and 24 more times innovation than large companies."[9]

They also say, "A study by the Office of Management and Budget shows that more than half the major technological advances of this century originated from individual inventors and small companies."[10]

II. GROWTH CAPITAL GAPS

A. Introduction

1. Definitions

All companies need growth capital — both equity and long-term debt, to finance their normal expansions. Large companies such as AT&T go to Wall Street regularly to sell stocks or bonds. When I was in business school, we learned theoretical formulas for determining whether it was time to raise either debt or equity.

Unfortunately, smaller companies do not have a choice — generally the decision is only of availability, not choice — as there are tremendous growth capital gaps for smaller businesses in our economy.

Moreover, the point is usually overlooked or misunderstood under the assumption that banks or the private sector will provide all the capital that a profitable business needs, or that highly publicized computer companies or "gene splicers," that are wooed by private venture capitalists, are typical of the financing stories of all small businesses.

A recent study by California's Department of Economic and Business Development stated, "A recurring concern...is the availability of capital

to support the establishment and growth of dynamic small manufacturers."[11]

Furthermore, the January 1981 issue of inc. magazine reported on a survey of 2,000 small businesses in which the "availability of long-term credit" was the third most important factor (out of 24) to small businesses in 1982.[12]

2. The Need

A growing small business needs long-term debt capital or equity capital for two primary needs:

a. Fixed Assets

Fixed assets, such as land and building, need to be financed by long-term financing, either as debt or equity. Short-term financing of 3-5 years for a new factory building is no more prudent than for a prospective home buyer.

b. Permanent Working Capital

Secondly, growing companies need permanent working capital in the business. A simple example makes the point. A growing company with annual sales of $1.2 million whose customers pay in 30 days needs $100,000 just to finance the receivables. If sales double to $2.4 million, then the company would need an extra $100,000 for expanded receivables — excluding additional capital needs for the cost of work in process. Some very "profitable" companies go bankrupt by growing too fast — due to this reason.

Tax cuts reduce the amount of money taken out of the business, but do not increase the new capital infusion into the business — which is the key need of a growing business.

B. Equity Capital

Growing smaller businesses usually start with equity investments from the founder/entrepreneur. They have difficulties obtaining equity capital for expansion. This section outlines the equity capital alternatives for smaller busineses ranging from informal risk capital from friends and neighbors to Wall Street investment bankers.

There really isn't much equity capital available to begin with. Mr. Reginald H. Jones, former Chairman and Chief Executive Officer of the General Electric Company, stated at the recent annual meeting of the American Council for Capital Formation, "In the decade of the 1960s, new equity provided only 1.5% of corporate cash sources. This grew to 5.6% in the first half of the 1970s but then fell sharply in the last half of the decade."[13] He predicted a figure of 3.4% during the '80s, most of which is for the nation's largest corporations — not growth capital for smaller businesses.

1. Informal Risk Capital

Most businesses start with money invested from the founder or his/her friends or associates. SBA's Office of Advocacy did a study of this source of capital which stated, "Informal investors are difficult to reach — geographically dispersed and tough to identify."[14] They also stated, "...the availability of essential risk capital (venture and equity capital to finance new and growing small firms declined steadily during the 1970 decade."[15]

2. Venture Capital

Venture capital is a phrase describing a variety of people and organizations including SBICs, private investors, corporations, etc. Venture capitalists are generally private sector investors looking for the "cream of the crop," the fast growing, most potentially profitable businesses. They do not finance the normal expansion needs of most smaller businesses. The September 1981 issue of Inc. magazine stated, "Organized venture capital will have little impact on the expansion capital needs of the vast majority of small businesses."[16]

In a section entitled "Expansion Capital: The Critical Issue," he stated, "Only a tiny fraction of the half million businesses started in the U.S. each year promise the kind of returns on invested money venture capitalists need."[17] In the same issue, Mr. Morton Collins, President of the National Venture Capitalists Association, states, "We are in the business of financing losses, not plant and equipment,"[18] i.e., venture capitalists are interested in fast growing start-ups and not moderate expansions needing plant and equipment.

David Brophy, Professor of Finance at the University of Michigan in Ann Arbor, Michigan, commented on Michigan's depressed economy and stated, "I compared Ann Arbor to Boston and Palo Alto because those are the two points of reference for technology-based industry. And as I visited there and talked with people, it appeared financing was the key element. Without local access to venture and growth money, the businesses just don't grow."[19] He cited the key difference between Michigan and Boston or Palo Alto respectively was that "Michigan's technology-based firms had to go out of the state to raise more of their venture capital."[20]

3. Investment Bankers

Investment bankers are the largest source of equity capital for large corporations, however they do not provide substantial equity capital for growing small businesses. An August 1981 study done by the SEC and SBA entitled "The Role of Regional Broker-Dealers in the Capital Formation Process: Underwriting, Market-Making and Securities Research Activities," pointed out that although the minimum initial public offering underwriting criteria of regional broker dealers was less than for national broker dealers, their standards still were too large for smaller businesses as their minimum dollar volume for an underwriting was $2.1 million, the minimum annual revenues for a client business was $4.4 million, the minimum net worth for a potenial business was $1.7 million, the minimum net profit was $600,000 and the minimum number of years incorporated was three years."[21]

The point is further made in a recent publication of the Donaldson, Lufkin and Jenrette Investment Banking concern where it describes its particular expertise in specific sectors including energy and emerging growth companies such as the computer, electronics or medical technology areas.[22]

4. Summary

Summarizing equity capital, although there are many players in equity and venture capital, most of them are chasing the cream of the crop and according to Inc. Magazine of September 1981, "The supply of expansion capital for small business has never been adequate in recent years and is less so today. The innovation and expansion capital gap will continue to be the critical problem for small business."[23]

C. Debt Capital

It is also difficult for most growing, profitable firms to obtain long-term debt capital for expansion.

1. Financial Institutions

None of the financial institutions are in the market for providing long-term debt capital for growth businesses.

a. Banks — All small businesses have bankers, yet bankers are short-term lenders — particularly in today's money market. Tax-exempt industrial revenue bonds, mostly bank loans in disguise, are helpful as they do reduce the interest rate.

b. Savings Institutions — Savings institutions were created to finance residential development, and in today's money market they are inactive.

c. Insurance Companies and Pension Funds — Insurance companies and pension funds are the primary source of long-term capital in the economy, however, they prefer larger projects — over $1 million.

Consequently, there is a long-term loan gap for smaller businesses in our economy.

2. First National Bank of Boston Study

The Council for Northeast Economic Action, an affiliate of the First National Bank of Boston, published a study in February 1981 entitled "An Empirical Analysis of Unmet Demands in Domestic Capital Markets in Five U.S. Regions."[24] Their survey was mailed to 30,000 business firms selected by five major banks, and the results confirm the growth capital gaps for smaller businesses. They concluded that there is a long-term credit gap for smaller businesses and that there may be as many as 50,000 viable smaller firms that have been unable to raise funds in the capital market.

3. Neighborhood Business Revitalization Program

The National Development Council's Neighborhood Business Revitalization program offers further evidence of the long-term debt capital for smaller businesses. In a four-year time period, the National Development Council was able to work in sixty cities and obtain long-term debt financing for 3,000 small and medium-sized businesses totaling $2.1 billion and creating over 130,000 private sector jobs. This figure really represents the tip of the iceberg rather than any saturation of the demand for long-term credit for viable businesses nationwide.

4. Small Business Investment Companies

Small Business Investment Companies (SBICs) are a tremendously important source of growth capital and include approximately 350 SBICs licensed by the SBA which in turn lend money to SBICs at preferred rates. SBICs have private investment from their owners and long-term debt from SBA. However, the report of the White House Commission on Small Business was concerned about the use of debt by SBICs and stated, "SBICs and minority enterprise SBICs in recent years have tended to relend their money to small companies at higher interest rates instead of investing in equity."[25]

5. Certified Development Companies

A newer program, designated specifically to provide long-term, subordinate debt for the fixed asset expansion needs of growing smaller businesses, is SBA's Section 503 Certified Development Company program. This program has been operative for approximately 10 months and has met tremendous demand for long-term debt capital by growing small businesses. In that time period, over 200 communities submitted applications to participate and 260 loans have been approved totaling approximately $40 million.

III. SUMMARY AND CONCLUSIONS

A. Summary

The growth capital needs of smaller businesses can be summarized by visualizing a pyramid in three tiers: Venture Capital, Risk Capital and Expansion Capital.

1. Venture Capital

The top layer is the cream of the crop of the venture capital business — very high risk, very few deals, very private sector and very high reward if you hit it right.

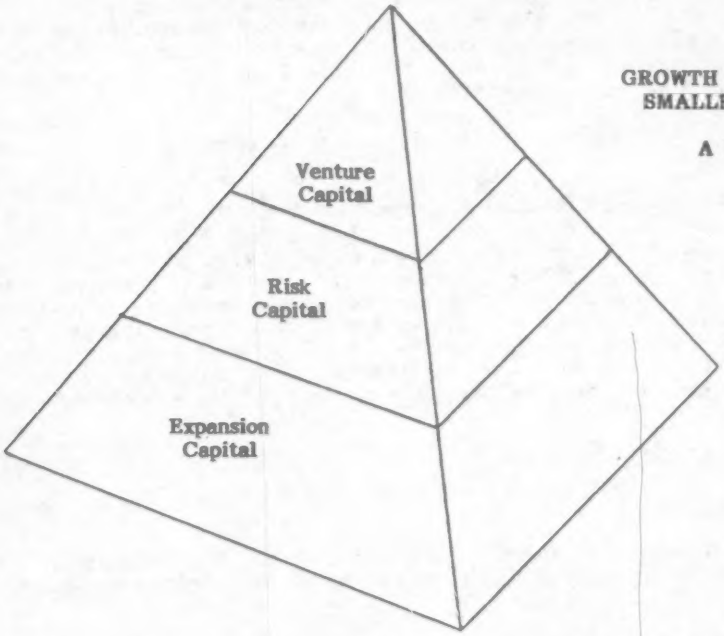
2. Risk Capital

The next "tier" of the pyramid might be called risk capital and includes both equity and debt investments by private investors for smaller businesses. Risk capital is predominantly private sector, although SBICs receive government guaranteed debentures. Investors in these businesses

do seek long-term growth — although not as risky perhaps as venture capital. The risk capital tier is larger than venture capital.

3. Expansion Capital

The third and bottom tier of the growth capital pyramid could be labeled "expansion capital," and is the area for the new SBA Section 503 program. CDCS, or Certified Development Companies, are public/private partnerships and are very important in the long-term creation of jobs in growing smaller businesses throughout the country. These long-term, fixed asset loans to expanding, profitable companies are not risky, and there isn't sufficient reward to invite venture or risk capital. This bottom tier of the pyramid is by far the largest.



GROWTH CAPITAL FOR SMALLER BUSINESS

A Pyramid

Tier	Risk	Reward	Volume of Business	Private or Public $
Venture Capital	Very High	Very High	Very Few	Totally Private
Risk Capital	Moderate	Moderate	Moderate	Mostly Private
Expansion Capital	Low	Low	Very Many	Public/Private

B. Cost Effectiveness

The SBIC and CDC programs indirectly use long-term government debt, which, contrary to common knowledge is declining relative to the GNP. The October 1981 issue of the newsletter from the American Council for Capital Formation quotes Professor Benjamin J. Friedman, Harvard Professor of Economics, in a study completed by the National Bureau of Economic Research, "Except only for 1975-76 and 1980, the Federal government has reduced its debt ratio every year since 1953."[26]

Also, the February 1, 1982 issue of Forbes states, "Fears that Federal borrowing will crowd out private borrowing are greatly exaggerated."[27]

The use of long-term government debt to leverage private debt and create permanent, private sector employment in expanding, successful small and medium-sized businesses must stand the test of cost effectiveness. What are the real costs of job creation in CETA, public service job programs, welfare, crime, supplemental unemployment insurance, etc.?

The Neighborhood Business Revitalization demonstration program created 132,584 jobs in 2,943 small and medium-sized businesses resulting from financing of $2.1 billion of capital investment. This results in one job created for each $15,616 of investment of which $13,199 is private capital and $2,417 is from the government. Hence, one permanent job can be created with a cost of $2,417 — which gets repaid with interest.

This is far more cost effective than the other programs which require $10,000-20,000 per year for each job — each year!

C. Conclusion

The November 2nd editorial of Business Week stated, "The facts are making it distressingly but unmistakably clear that the economy is not responding as hoped."[28] The supply side surge is slow in coming.

Our policy conclusion is as follows: All companies need capital investment to grow, to create jobs, to pay taxes and to increase the competitiveness and productivity of the American economy. Smaller businesses are a primary source of that growth and job creation but they are not the focus of policy — particularly regarding the availability of growth capital which, as outlined above, is not very available from the wide variety of sources of capital in the American economy.

Statistics from the SBIC, Section 503 CDC and Neighborhood Business Revitalization programs show that policies and programs to create jobs and stimulate the economy are far more cost effective than other employment programs. However, more attention and stronger policies and programs to provide growth capital for smaller businesses are needed. The same is true in Britain. A recent Economist article on the growth of high technology companies in Britain laments, "Many high tech companies have come to grief (or never got off the ground) through lack of finance."[29]

In a chapter entitled "The Imperatives of Growth," George Gilder summarizes, "Those smaller corporations with less access to loans, no access to equity markets...suffer more obviously (from inflation and excessive regulation)."[30]

His policy reommendation is: "If the United States diverts the proceeds of its inflation tax into the creative core of capitalist growth — the new research and industry of the future — both the problem of inflation and the problem of growth will disappear."[31]

Stronger policies and programs providing growth capital for smaller businesses, such as the 503 program, are the essence of that policy.

John Sower
Washington, D.C.

FOOTNOTES

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2. Economist, October 3, 1981, page 22.
3. Inc. Magazine, October 1981.
4. "The Education of David Stockman," William Greider, The Atlantic, Vol. 248, No. 6, December 1981, page 46.
5. "Venture Capitalists Get Bolder," Business Week, November 30, 1981, page 101.
6. "Report of the Study Group," Conservative Parliamentary Backbench Industry Committee, Mr. Michael Grylls, M.P., London, England, October 1981.
7. David L. Birch, "The Job Generation Process," M.I.T., Cambridge, Massachusetts, page 8.
8. George Gilder, Wealth and Poverty, Basic Books, New York, 1981, page 83.
9. America's Small Business Economy, White House Commission on Small Business, April 1980, page 20.
10. Ibid., page 21.
11. "Financial Performance, Growth and Financing for Small Manufacturers," Office of Economic Policy, Planning and Research, California Department of Economic and Business Development, May 5, 1981, page 1.
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14. "Informal Risk Capital in New England," William E. Wetzel, Jr., Whittemore School of Business and Economics, and Craig R. Seymour, Center for Industrial and Institutional Development, University of New Hampshire, Durham, New Hampshire, January 1981, page 62.
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16. Christopher A. Leach, "The Billion Dollar Gamble," Inc. Magazine, September 1981, page 58.
17. Ibid., page 60.
18. Ibid., page 61.
19. David Brophy, "Financing for Technology Is Scarce Here," Ann Arbor News Special Technology Supplement, April 10, 1981, page 16.

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21. "The Role of Regional Broker-Dealers in the Capital Formation Process: Underwriting, Market-Making and Securities Research Activities," SEC and SBA, August 1981, pages 23 and 24.

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23. Inc. Magazine, September 1981, page 60.

24. "An Empirical Analysis of Unmet Demands in Domestic Capital Markets in Five U.S. Regions," Council for Northeast Economic Action, Boston, Massachusetts, February 1981.

25. White House Commission on Small Business, page 69.

26. American Council for Capital Formation, "Capital Formation," Vol. 6, No. 9, October 1981, page 8.

27. Forbes, "Why the Disaster Scenario Is Wrong," Edited by Thomas O'Donnell, page 25.

28. Business Week, "Editorials," Noember 2, 1981, page 156.

29. "Britain's Sunrise Strip," The Economist, January 30, 1982, page 73.

30. George Gilder, Wealth and Poverty, page 223.

31. Ibid., page 231.

Mr. MITCHELL. Mr. Smith, before you give your testimony, let me assure you that the selection of witnesses was done purely on an objective basis. It is just by sheer accident that we have some Baltimorians represented here. Larry, it is good to see you.

TESTIMONY OF LARRY SMITH, SENIOR VICE PRESIDENT, BALTIMORE ECONOMIC DEVELOPMENT CORP.

Mr. SMITH. It is good to see you, too, Congressman.

It really is a pleasure to be here today to speak for the Baltimore Economic Development Corp. to you and the members of the committee on behalf of the continuation and expansion of present levels of the SBA 503 program.

I would like to take a brief minute to familiarize you with the Baltimore Economic Development Corp., our essential mission, and our reason for being in existence, and give you just a brief overview of the recent success we have enjoyed.

BEDCO was formed in 1976 by the mayor and city council of Baltimore to serve as its agent for economic development, specializing in industrial development in the city of Baltimore. Since that time it has been more than successful in accomplishing its essential goals of improving the employment opportunities for the constituency of the city of Baltimore, as well as strengthening the municipal tax base.

We have been able to accomplish these missions, essentially through three avenues of activities. BEDCO provides essentially a one-stop service for businesses seeking plant locations, as well as project financing, assistance in dealing with Government regulations or obtaining services from the city government.

Also, BEDCO encourages the growth of industrial and commercial firms by offering financial incentives and technical services to facilitate their location or expansion in the city of Baltimore. And, third, BEDCO actually acquires and develops industrial real estate to maintain a ready and diverse inventory of sites and facilities available to BEDCO clients and those seeking assistance of that nature in the city of Baltimore.

BEDCO was certified or approved as a certified development corporation by the SBA in January 1981. In this 16-month period we have been involved in approving 15 loans, totaling $5,862,000; involving leveraged public funds of $2,251,000 for private equity investments, with city investment making up the balance of $3,532,000. These funds, as stipulated in the 503 SOP, have been used for the purpose of acquiring land, acquiring buildings, renovating existing structures, as well as for the purchase of machinery and equipment for specialized use in various manufacturing operations.

I might also add that the use of these funds in these 15 projects actually does represent a cross section of the diverse Baltimore economy, with projects ranging from renovation of shopping centers, expansion of manufacturing facilities, redevelopment of a run-down downtown hotel, and restaurants. It just runs the gamut, so we have been quite pleased with the diversity of the operation.

The benefits across the board to this diverse group of entrepreneurs have been fairly consistent in providing below-the-market-rate financing, which is absolutely essential for the success of many of these projects, as well as long-term, fixed-rate financing, which is quickly becoming a dinosaur in today's economy.

It also enhances the banking relationships which are so essential to growing and maturing small businesses by increasing the collateral base. Private lending institutions have been more inclined to participate in these projects.

The job creation impact has been significant. Of the 15 projects, jobs retained amounted to 430. New jobs created were something under 300; 261 jobs. To that end, the SOP of the 503 program suggests that there be one job created for every $15,000 of investment. We feel very proud that in our 15 we have created one job for every $3,200 invested.

If there is a problem area in the 503 program, aside from the normal startup administrative problems, which every program experiences from time to time, it has been a recent change in the term of the loans. Initially, a minority portion of the loan could be for a term as short as 5 years. The exposure has been more than doubled with the recent revision of the SOP to 10 years.

There also happens to be in the revised SOP prohibition of owner loans of the 50 percent portion. Any time you lose any degree of flexibility, it could put the project in jeopardy, but I will emphasize that these are not major problem areas that cannot be overcome in most cases.

We project that the 503 program is and will continue to be one of the most viable economic development tools in the financing area that BEDCO has available to it at this time. At present we have 10 projects in our pipeline. The total of these projects is $3 million. The 503 portion would be $1,200,000 approximately. By year end,

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we expect to have closed $4 million in 503 projects creating or retaining approximately 450 jobs.

I would like to just give you one quick, brief example of the leveraging effect of the 503 program, as we have been using it in Baltimore.

There was recently a request made by a well-established restaurant in Baltimore to its bank, with which it had enjoyed a long and prosperous banking relationship, for an $850,000 loan to expand its operations and increase its employment. The bank was reluctant to do the deal. We got involved and were able to provide $320,000 through the 503 program, and $60,000 through city funds. This enabled the entrepreneur to leverage their $130,000 in equity for a bank loan of $345,000. The bank was well pleased. Their collateral position was tremendously improved and we are reasonably expecting this to be a very successful operation.

The 503 program has been probably more widely used and it is definitely one of the first considerations as a financing vehicle at BEDCO in the city of Baltimore, second only to the industrial revenue bond financing. With the uncertainty of the continued regulations and guidelines concerning the industrial revenue bond financing, we would recommend that this committee continue and expand the 503 program, as it would represent a very viable alternative should IRB's be discontinued or reduced.

Thank you.

[The prepared statement and attachment of Mr. Smith follow:]

Prepared Statement of Larry Smith, Senior Vice President, Baltimore Economic Development Corp.

MR. CHAIRMAN, MEMBERS OF THE COMMITTEE AND GUESTS, IT IS MY PLEASURE TO SPEAK TO YOU TODAY FOR THE BALTIMORE ECONOMIC DEVELOPMENT CORPORATION ON BEHALF OF CONTINUATION AND EXPANSION OF PRESENT LEVELS OF SBA 503 FUNDING. FIRST, I WOULD LIKE TO FAMILIARIZE YOU WITH THE OPERATIONS OF THE BALTIMORE ECONOMIC DEVELOPMENT CORPORATION (BEDCO) AND HOW IMPORTANT THE 503 PROGRAM IS AS PART OF OUR COMPREHENSIVE PROGRAM TO ASSIST BUSINESSES IN BALTIMORE.

THE BALTIMORE ECONOMIC DEVELOPMENT CORPORATION (BEDCO) IS A QUASI-PUBLIC NON-PROFIT ORGANIZATION CREATED IN JANUARY, 1976 BY THE MAYOR AND CITY COUNCIL OF BALTIMORE TO ACT AS THE CITY'S AGENT FOR ECONOMIC DEVELOPMENT, WITH EMPHASIS ON INDUSTRIAL DEVELOPMENT, IN ORDER TO IMPROVE EMPLOYMENT OPPORTUNITIES AND STRENGTHEN THE MUNICIPAL TAX BASE.

THIS IS ACCOMPLISHED IN THREE WAYS:

1. BEDCO PROVIDES A "ONE-STOP" SERVICE FOR BUSINESSES SEEKING A PLANT LOCATION, PROJECT FINANCING, ASSISTANCE IN DEALING WITH GOVERNMENTAL REGULATIONS OR OBTAINING SERVICES FROM CITY GOVERNMENT.

2. BEDCO ENCOURAGES THE GROWTH OF INDUSTRIAL AND COMMERCIAL FIRMS BY OFFERING FINANCIAL INCENTIVES AND TECHNICAL SERVICES TO FACILITATE THEIR LOCATION OR EXPANSION IN BALTIMORE.

3. BEDCO ACQUIRES AND DEVELOPS INDUSTRIAL REAL ESTATE TO MAINTAIN A READY AND DIVERSE INVENTORY OF SITES AND FACILITIES AVAILABLE TO A BROAD SPECTRUM OF INDUSTRIAL USERS.

SINCE 1976, BEDCO HAS EITHER RETAINED OR CREATED OVER 20,000 JOBS THROUGH ITS FINANCIAL AND DEVELOPMENT OPERATIONS. IN ALL, BEDCO WILL BE RESPONSIBLE FOR OVER 400 ACRES OF INDUSTRIAL DEVELOPMENT. AT PRESENT, 160 ACRES HAVE BEEN SOLD OR OPTIONED TO FIRMS INVESTING $38 MILLION AND EMPLOYING OVER 2,100 PEOPLE.

DURING 1981, BEDCO PARTICIPATED IN ARRANGING FINANCING FOR 79 COMPANIES INVOLVING $200.8 MILLION OF CAPITAL INVESTMENT. OF THIS AMOUNT, $65 MILLION WAS USED FOR A PORT DEVELOPMENT REVENUE BOND TO FINANCE COAL EXPORT FACILITIES. THE 69 EXISTING AND 10 NEW COMPANIES ASSISTED BY BEDCO WILL BE EMPLOYING 8,000 WORKERS AFTER COMPLETION OF THE IMPROVEMENTS FINANCED BY THESE LOANS--AN INCREASE OF 60% OVER THEIR PRE-LOAN STATUS--OR APPROXIMATELY 3,000 NEW JOBS. ANNUAL REAL PROPERTY TAX REVENUES FROM BEDCO-ASSISTED PROJECTS WAS ESTIMATED AT $2 MILLION IN 1981 AND WILL CLIMB FURTHER IN FUTURE YEARS.

BEDCO WAS CERTIFIED AS A SMALL BUSINESS ADMINISTRATION (SBA) 502 LOCAL DEVELOPMENT CORPORATION (LDC) IN SEPTEMBER 1977. THE LDC WAS INCORPORATED AS THE BEDCO DEVELOPMENT CORPORATION. IN JANUARY, 1981, THE BEDCO DEVELOPMENT CORPORATION WAS APPROVED AS AN SBA 503 CERTIFIED DEVELOPMENT CORPORATION (CDC).

SINCE BEDCO DEVELOPMENT CORPORATION'S CERTIFICATION AS A CDC, 15 SBA 503 LOAN REQUESTS HAVE BEEN APPROVED. THE 503 LOANS, TOTALING $2,251,000, OR 38% OF THE TOTAL ELIGIBLE PROJECT COST, LEVERAGED $3,532,000 IN OTHER INVESTMENTS, INCLUDING $2,007,000 FROM FINANCIAL INSTITUTIONS, $947,000 IN EQUITY

INVESTMENT AND $611,000 FROM CITY LOAN FUNDS. (SEE ATTACHED TABLE.) THE TOTAL INVESTMENT REPRESENTS ONLY ELIGIBLE PROJECT COSTS--PURCHASE OF LAND AND BUILDINGS, RENOVATION OF EXISTING STRUCTURES AND PURCHASE OF EQUIPMENT. IF OTHER TYPES OF FINANCING NOT CONSIDERED ELIGIBLE UNDER THE 503 PROGRAM ARE INCLUDED--SUCH AS WORKING CAPITAL FINANCING FOR ACCOUNTS RECEIVABLE, INVENTORY, SALARIES, ETC.--THE 503 PORTION, IN EFFECT, LEVERAGED A MUCH GREATER AMOUNT OF PRIVATE SECTOR FUNDING.

WHEN COMPLETED, THE 15 SBA 503 PROJECTS WILL RETAIN 430 JOBS AND CREATE 261 NEW JOBS--A TOTAL OF 691 JOBS IMPACTED BY THE PROGRAM OR AN INVESTMENT OF 1 JOB FOR EVERY $3,258 SBA 503 DOLLARS INVESTED--CONSIDERABLY LESS THAN THE $15,000/JOB REQUIREMENT SPECIFIED IN 503 SOP.

THE PROJECTS APPROVED BY THE BEDCO DEVELOPMENT CORP. REFLECT THE VARIETY OF THE BALTIMORE ECONOMY--4 MANUFACTURING FIRMS, 3 RESTAURANTS, 5 RETAIL OUTLETS, ONE HOTEL, ONE PROFESSIONAL OFFICE, AND ONE CLEANING SERVICE. TWO OF THE PROJECTS ARE MINORITY-OWNED AND OPERATED. TO DATE, 2 DEBENTURES HAVE BEEN SOLD BY THE FEDERAL FINANCING BANK.

CURRENTLY 10 DEALS ARE IN PROCESS REPRESENTING OVER $3,000,000 IN TOTAL INVESTMENT LEVERAGED BY $1,230,000 IN 503 LOANS. APPROXIMATELY 450 JOBS WILL BE RETAINED OR CREATED.

DURING 1981, APPROXIMATELY $2.2 MILLION IN 503 LOANS WERE APPROVED BY THE BEDCO CDC. BASED ON CURRENT LEVELS OF ACTIVITIES AND CONTINUING HIGH INTEREST RATES, WE EXPECT TO APPROVE BETWEEN $3 MILLION AND $4 MILLION WORTH OF 503 LOANS IN 1982.

THE 503 PROGRAM IS ONE OF THE MOST VERSATILE TOOLS AVAILABLE TO HELP LOCAL COMPANIES EXPAND AND GROW. NEXT TO TAX-EXEMPT FINANCING, THE 503 PROGRAM HAS BEEN OUR MOST WIDELY USED FINANCIAL INCENTIVE.

THE 503 PROGRAM OFFERS BELOW MARKET RATE, LONG TERM FINANCING TO SMALL BUSINESSES WHO OTHERWISE WOULD NOT BE ABLE TO GO FORWARD WITH THEIR PROJECTS DUE TO CURRENT LEVELS OF HIGH INTEREST RATES AND/OR BECAUSE BANKS ARE UNWILLING TO FINANCE THE TOTAL AMOUNT. THE PROGRAM IS NOT INTENDED FOR WEAK FIRMS OR BAIL-OUT SITUATIONS--THE FIRMS HAVE TO DEMONSTRATE THE ABILITY TO REPAY THE LOANS BASED ON THEIR PAST PERFORMANCE, MANAGEMENT EXPERIENCE AND REASONABLENESS OF PROJECTIONS.

THE 503 PROGRAM IS INTENDED ONLY FOR PERMANENT FINANCING. SINCE BANKS HAVE TO PROVIDE INTERIM FINANCING FOR PROJECT COMPLETION, WHICH IS NOT GUARANTEED BY THE SBA, THE BANKS HAVE TO BE REASONABLY SATISFIED THAT THE COMPANY WILL CARRY OUT THE PROGRAM WITHOUT UNEXPECTED ADVERSE CHANGES AND SIGNIFICANT COST OVERRUNS. THIS PROVIDES A DOUBLE PROTECTION AGAINST MAKING LOANS TO LESS THAN VIABLE COMPANIES.

IT WOULD BE SAFE TO SAY THAT MOST, IF NOT ALL, OF THE PROJECTS APPROVED BY THE BEDCO CDC WOULD NOT HAVE GONE FORWARD WERE IT NOT FOR THE INJECTION OF THE 503 PORTION OF THE FINANCING. SEVERAL EXAMPLES WILL PROVE THIS POINT. INITIALLY, A BANK WAS NOT WILLING TO APPROVE AN $800,000 LOAN TO A RESTAURANT FOR EXPANSION AND RENOVATIONS. WITH THE 503 PROGRAM PROVIDING $320,000 IN BELOW MARKET RATE, LONG TERM FINANCING, THE BANK WAS WILLING TO MAKE A LOAN FOR $345,000 SINCE OVERALL DEBT PAYMENTS WERE CONSIDERABLY REDUCED AND THEIR COLLATERAL POSITION WAS IMPROVED BY THE SECOND LIEN POSITION TAKEN BY THE 503 LOAN. FOR A MANUFACTURING FIRM, A BANK WAS RELUCTANT TO LOAN MONEY FOR PURCHASE OF SPECIALIZED EQUIPMENT THAT HAD GREAT VALUE TO THE COMPANY BUT POTENTIALLY LITTLE VALUE TO OTHER USERS. THE 503 PROGRAM WAS ABLE TO FINANCE THE EQUIPMENT PORTION OF THE EXPANSION PROGRAM. THE 503 PROGRAM IS FINANCING RENOVATIONS AND IMPROVEMENTS TO A MINORITY-OWNED NEIGHBORHOOD SHOPPING CENTER

IN A STABLE BLACK COMMUNITY WITH 80% HOME OWNERS. THE CENTER WAS INFESTED WITH RODENTS; MOST OF THE BUILDINGS WERE BOARDED UP, AND THE PARKING LOT WAS FILLED WITH POTHOLES. THE SITE WAS AN EYESORE AND A BLIGHTING INFLUENCE ON AN OTHERWISE HEALTHY COMMUNITY. BANKS WERE RELUCTANT TO LEND MONEY FOR THIS PURPOSE BECAUSE OF THE CENTER'S CONDITION AND LOCATION. THE SHOPPING CENTER IS NOW BEING RENOVATED AND CLEANED UP BY THE OWNER OF THE EXISTING VARIETY STORE WITH ASSISTANCE OF A 503 LOAN, CITY LOAN, $75,000 BANK LOAN AND $195,000 IN EQUITY INVESTMENT--THE EQUITY REPRESENTS 28% OF THE TOTAL PROJECT. BESIDES THE VARIETY STORE, A SUPERMARKET AND SEVERAL CONVENIENCE-TYPE STORES WILL BE TENANTS. THE 503 PROGRAM ALSO HELPED FINANCE THE RENOVATION OF A RUNDOWN, DOWNTOWN HOTEL, A PROJECT THAT WAS NOT FEASIBLE AT MARKET INTEREST RATES.

THE 503 PROGRAM, THUS, IS SORELY NEEDED IN TODAY'S ECONOMY TO PROMOTE INVESTMENT BY SMALL FIRMS FOR EXPANSION AND MODERNIZATION. WHEN WORKING CAPITAL FINANCING IS INCLUDED, THE 503 PROGRAM IS ABLE TO LEVERAGE OUT OF GOVERNMENT RESOURCES A MUCH GREATER PROPORTION OF PRIVATE SECTOR INVOLVEMENT THAN INDICATED BY TOTAL ELIGIBLE PROJECT COST. IN BALTIMORE THE PROGRAM HAS FUNDED 15 PROJECTS TOTALING OVER $5.8 MILLION IN INVESTMENT AND RETAINING OR CREATING NEARLY 700 JOBS. THE PROGRAM SHOULD BE CONTINUED AND FUNDING LEVELS EXPANDED SINCE IT ENCOURAGES FINANCIAL INSTITUTIONS AND PRIVATE INVESTORS TO INVEST MONEY IN SMALL BUSINESSES. THESE ARE THE FIRMS THAT STUDIES HAVE SHOWN ARE RESPONSIBLE FOR THE GREAT PROPORTION OF NEW JOB CREATION.

I THANK YOU FOR YOUR TIME AND CONSIDERATION.

BEDCO DEVELOPMENT CORPORATION - SBA 503 PROGRAM

Minority Owned	Name of Company	Type	Structure of Financing (000's) Total Investment	503	City	Private	Equity	Employment Retained	Employment New	Date Appoved by CDC	Date Debenture Sold
	Princess Shops	Retail	$380	$125	$75	$150	$30	7	8	11/80	
X	Sony's Kitchen	Restaurant	189	78	82	--	29	--	15	2/81	
	Sabatino's	Restaurant	855	320	60	345	130	52	25	2/81	4/82
X	Oliver St. Plaza	Retail	696	275	150	75	195	14	16	7/81	
	Sonitrol	Mfg. Security Systems	359	116	10	172	61	34	15	4/81	
	Howard House	Hotel	1,085	420	--	556	108	22	20	9/81	4/82
	Wells Liquors	Retail	292	116	10	112	54	--	10	9/81	
	P & G Partnership	Professional office	361	140	--	110	111	12	18	9/81	
	Baltimore Rebuilders	Mfg.-auto parts	114	57	--	50	7	70	15	11/81	
	Inner Harbor Lumber	Retail/ warehouse	200	80	50	--	70	15	10	11/81	
	Total Janitorial	Service	142	56	25	45	16	150	30	11/81	
	Swan Secure Products	Mfg.-nuts & bolts	97	39	--	--	58	--	15	11/81	
	Hammerjacks	Bar	705	282	64	280	79	30	55	12/81	
	Katzenstein	Retail	154	60	65	--	29	6	3	12/81	
	Performance Bindery	Mfg.-bindery	233	93	20	112	8	18	6	12/81	
	Totals		$5,862	$2,251	$611	$2,007	$985	430	261		

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Mr. MITCHELL. Thank you very much.

Mr. Matteo is our next witness.

Mr. MCDADE. Mr. Chairman, I want to welcome Vince here today. He is a very vital and active person in my chamber staff group and I guess this may be your first time testifying in Washington. I am not sure, but whether it is or not, welcome. We are glad to have you here.

TESTIMONY OF VINCENT J. MATTEO, DIRECTOR OF GOVERNMENT AFFAIRS AND SMALL BUSINESS DEVELOPMENT, GREATER SCRANTON CHAMBER OF COMMERCE, AND METROACTION, INC.

Mr. MATTEO. Thank you, Congressman, and I am sure it is a coincidence that the ranking minority member's district is speaking second.

I am Vincent Matteo, the director of small business development for the Greater Scranton Chamber of Commerce and an affiliate organization, MetroAction, Inc. I would like to thank you for the opportunity of testifying here today on what we believe is a very important program for the future of Lackawanna County, the 503 program.

I am talking to you from perhaps a different perspective than the other gentlemen here today, because MetroAction has not yet received its 503 certification. We are in the pipeline in Washington and it is moving along very well.

I have prepared written testimony, which has already been submitted and at this time I would like to basically summarize it and add, perhaps, a few other points.

I discuss in the written testimony that the chamber of commerce in Scranton has a long history of excellence in industrial development. For example, in 1981, the chamber, through its industrial development arm, SLIBCo, which is the Scranton-Lackawanna Industrial Building Co., administered over 40 active projects, with an original cost of $70 million. There are 14,500 people employed at these projects with an annual payroll of over $213 million. SLIBCo utilizes funds from the Pennsylvania Industrial Development Authority. Yet, despite the impressive record that the SLIBCo-PIDA partnership has set, there is a void in our own development program and that void is in assisting small business. Unfortunately, small business is being hit hardest by the current uncertain economic conditions. The result has been an added pressure on Lackawanna County's unemployment rate. As of February of this year, the rate was at 11.3 percent and, obviously, that is unacceptable.

The No. 1 problem facing our small business people is the lack of available money. We believe that that void can be filled by the 503 program. Because of this belief, MetroAction has an application pending with the SBA for designation as a 503 corporation. We believe the 503 program will fit well into our overall development activities.

With the 503 program, we will be in a position to assist both manufacturing and commercial small businesses that we cannot now assist. One advantage of the 503 program is that we will be able to lend money for machinery and equipment, something we

cannot do with Pennsylvania Industrial Development Authority (PIDA). In addition, MetroAction is committed to the revitalization of downtown Scranton, as well as the business districts of our smaller communities.

The 503 program will stimulate the type of small business investment necessary to accomplish this goal, but the most important benefit is, of course, the jobs that we know it will create.

In concluding, let me stress that we are not asking for anything that we have not already committed our own resources to. The chamber, MetroAction, and its other affiliated organizations have committed in excess of $500,000 to our 1982–83 development budget and 20.6 percent of our chamber's membership dues goes directly to my small business development program. These may not be large numbers in Washington terms, but it is a very significant local commitment. We are committed, as our Congressman is, to small business in Lackawanna County.

The PIDA program was based on the now famous Scranton plan for industrial development and 503 was patterned after PIDA, so we know how to use 503. Therefore, we strongly urge you to continue and expand the 503 program.

Thank you.

[The prepared statement of Mr. Matteo follows:]

PREPARED STATEMENT OF VINCENT J. MATTEO, DIRECTOR OF GOVERNMENTAL AFFAIRS AND SMALL BUSINESS DEVELOPMENT, GREATER SCRANTON CHAMBER OF COMMERCE, AND METROACTION, INC.

Mr. Chairman, members of the Committee, I am Vincent J. Matteo, the Director of Small Business Development for the Greater Scranton Chamber of Commerce and its affiliated organization, MetroAction, Inc. I would like to express my appreciation to the Committee for the opportunity to speak to you today on a matter of significant importance. Before proceeding to the main body of my testimony, I would like to give you some brief background on myself.

I am a graduate of Wilkes College, in Wilkes-Barre, Pennsylvania where I received a B.A. degree in Political Science. I am currently preparing for my final oral examinations for the degree of Doctor of Public Administration.

I have been employed by the Greater Scranton Chamber of Commerce since January of 1980. I was hired to develop a governmental affairs program and to establish a Small Business Development program for the Chamber.

Prior to my joining the Chamber, I was employed from 1975 to 1978 by the Pennsylvania Manufacturers Insurance Association and from 1978 until joining the Chamber, I served as the Executive Director of the Susquehanna River Basin Association, a non-profit citizens organization headquartered in Wilkes-Barre, Pennsylvania.

Representing some 1,500 businesses, the Greater Scranton Chamber of Commerce operates throughout Lackawanna County. It offers the business community and residents a unified cohesive program designed to promote industrial development, improve the quality of life and create jobs. The Chamber maximizes its efforts by coordinating its industrial activities through several umbrella organizations. These are the Scranton Lackawanna Industrial Building Company (SLIBCo), the Lackawanna Industrial Fund Enterprises (LIFE), the Scranton Industrial Development Company (SIDCo), and MetroAction, Incorporated.

Strategically located at the conversion of five major highways, I-81, I-84, I-80, I-380 and the Northeast Extension of the Pennsylvania Turnpike, Scranton is the center of the three county region of Lackawanna, Luzerne and Monroe, which is defined as the Northeastern Pennsylvania Standard Metropolitan Statistical Area.

Scranton and Lackawanna County has a long, proud history. Its name synonymous with that of coal, the area was first settled in the 1700's. Since that time, the region has experienced a number of serious economic problems. Each time, however, the residents of the region have worked together to overcome the adversity. This first started in 1915 with the creation of SIDCo with a capital investment of $1.2

million dollars. This was the beginning of what has become nationally known as the Scranton Plan.

Perhaps the efforts of the Chamber had its finest hours immediately following World War II. Following the closing of a major employer in the county, the Chamber and the citizens raised $1,200,000 to purchase the plant and have it reopened. Following this success story, another fund drive took place in 1946. Launched by the Scranton Lackawanna Industrial Building Company, the goal was to broaden the base laid by the Scranton Plan by building "shell" plants for future industry. This drive brought in $931,000 and local banks contributed an additional $1 million. Two years later, SLIBCo launched another campaign which realized an additional $261,000.

Despite this success, the region suffered with the total collapse of the coal industry. Between 1940 and 1950 some 15,000 miners were put out of work. As a result, the first county-wide industrial development effort was initiated. The creation of the Lackawanna Industrial Fund Enterprises resulted in a fund drive which raised $1.3 million in just a few weeks. The Scranton Plan method of financing plant construction for industries was successful, however, it was limited in that it only included local money.

In 1956, the Pennsylvania Industrial Development Authority (PIDA) was formed. This greatly increased our resources. Based upon the Scranton Plan, PIDA, an agency of the Commonwealth, provides second mortgage loans at a low-interest rate for building and land projects. These funds are made available through Development Companies for the economic advantage of manufacturing companies who will provide substantial direct industrial employment opportunities. SLIBCo utilizes this method of financing for new plant construction, as well as, acquisition for the benefit of companies new to Pennsylvania and also to facilitate expansion of established industry. Financing through PIDA is predicated on Project Cost as follows: Building and land via SLIBCo/PIDA which provide for:

1. A bank first mortgage in amount of 50 percent of the Project Cost at prevailing interest rates.

2. A PIDA second mortgage in the amount of 50 percent of the Project Cost at 5 percent for a term of 15 years (if the industry has a total employment of less than 50 people, the PIDA second mortgage participation can be increased to 60 percent of the Project Cost)

SLIBCo by Agreement will act as Agent for the industry in applying for proposed mortgages, all legal matters pertaining to the project, bidding and constructing the plant to a company's approved plans and specifications, disbursement of project funds, etc. SLIBCo holds title to the property until completion of construction and through the term of the Lease until such time as the industry whould exercise its option.

SLIBCo/PIDA funding is available for all manufacturing enterprises as well as for companies classified as warehouse/distribution in nature with a minimum total project cost of $250,000 and 25 new jobs, a building which houses the executive national headquarters of a company or conglomerate which has facilities in more than one state, a regional headquarters which houses the branch executive offices of a national company, a building which houses computer and keypunch operations of a company and a building which houses clerical operations for some or all of the executive and administrative offices of a company and the operations.

The SLIBCo/PIDA partnership has been tremendously successful in Lackawanna County. Utilizing PIDA funds as part of comprehensive economic packages offered to companies, the Chamber, through SLIBCo, has already assisted 91 companies in 134 separate projects. The annual payroll of the estimated 14,500 persons working in SLIBCo sponsored, PIDA financed industries total $213,000,000. In 1981 alone, SLIBCo administered over 40 active projects with a total original cost of $70 million. SLIBCo projects account for $18,786,198 in assessed property valuations. This is over 5 percent of all of Lackawanna County's assessed valuation.

Despite his impressive record, the Chamber and its development companies realize that a serious void in assisting a major segment of our business community exists the Small Business. I need not recount the facts concerning the importance of small business to our nation's economy nor the trouble that small business is facing. The facts applicable to the nation's small business community are just as applicable to Lackawanna County's small business community. Lackawanna County's unemployment rate as of February, 1982 is 11.3 percent. Unfortunately, the economic climate has resulted in the failure of many small businesses, thus contributing to this rate. Because of the importance of small business, the Chamber has embarked upon an impressive program to assist them. The Chamber has committed thousands of dollars and full-time staff to assist small business. Our total development budget for

1982-83 is in excess of $500,000 and 20.6 percent of our Chamber's membership dues is invested in our Small Business Development Program. Although these may be small amounts in dollar terms of Washington, they represent a substantial local commitment. The Chamber has established a Small Business Council which offers a variety of services ranging from individual counseling to seminars. However, the bottom line in these troubled economic times is, as you are well aware, available money. This is where the void exists. The requirements for PIDA funds make it virtually impossible to loan money to most small, non-manufacturing firms. Yet, these are the very businesses which need the most assistance. The Chamber believes, however, that this void can be filled. This mechanism available to fill it is the SBA 503 CDC Loan Program. Patterned after the Pennsylvania Industrial Development Authority program, SBA 503 is seen by our community leaders as a major tool in assisting the expansion and growth of small business in Lackawanna County.

Currently, MetroAction, Inc., one of the Chamber's development organizations, which was originally created to spur downtown revitalization in Scranton, has an application pending in Washington with the SBA which would designate MetroAction as a 503 CDC. MetroAction has also applied for membership in NADCO. If granted, MetroAction would utilize the 503 Program to assist small businesses, both manufacturing and non-manufacturing, throughout the counties of Lackawanna, Luzerne and Monroe. We also believe it would assist the massive efforts to revitalize downtown Scranton and the business districts of small communities. MetroAction is committed to making the 503 Program the "PIDA" program of small business in Lackawanna County. Utilizing 503, we believe we can make it possible for our area's small business community to prosper and grow. This will result in positive economic growth and new jobs whose affect will be felt throughout our entire region.

Because of this belief, we are here to add our voice to the many communities, civic organizations and businesses throughout the nation who are calling for continued and proper funding for the 503 Loan Progam. It is a program that is desperately needed in Northeastern Pennsylvania. It is a program that has already begun to assist other areas throughout the nation. It is a program that deserves the support of this body.

Therefore, we strongly urge you to support continued adequate funding for the 503 Loan Program. This will be a major step in turning the fortunes of small business around and putting our people back where they belong—to work. Thank you.

Mr. MITCHELL. Thank you.

I'll just ask staff a quick question: What is the level of funding this year for the 503 program? Do you know offhand?

Mr. POWERS. $250 million.

Mr. MITCHELL. And what was it last year?

Mr. POWERS. No change.

Mr. MITCHELL. No change. So, it seems to me in light of the rate of unemployment, we ought to be considering a change.

Mr. SOWER. Congressman, may I comment?

Mr. MITCHELL. Yes.

Mr. SOWER. The funding level has been a confusing issue, frankly, for this year and for next fiscal year between the administration's proposals, the continuing resolution issues, the proposals from the House of Representatives and the Senate. So, it has been a confusing issue.

Mr. MITCHELL. But SBA is at $150 million.

Mr. SOWER. That is the level stated by SBA for the present fiscal year. Yes, sir.

Mr. MITCHELL. Thank you.

Mr. Albertson, please.

TESTIMONY OF DON J. ALBERTSON, EXECUTIVE VICE PRESIDENT, IOWA BUSINESS GROWTH CO.

Mr. ALBERTSON. Mr. Chairman, I thank you for giving me the opportunity to appear here and give testimony. The level of funding is the main reason that I am here.

I am Don Albertson, executive vice president of Iowa Business Growth Co. We have the first nationwide certified development company approved by SBA. I have submitted written testimony and I would like to just very briefly summarize what is in this testimony.

We were certified by SBA in May 1981. Upon certification, we took care of some of the final organizational requirements, gave news releases to the media and were able to appear on several financing seminars in the State. This resulted in our receiving numerous inquiries. To date, we have received 320 documented inquiries on the 503 program. We approved our first project in August 1981 and, to date, have approval by SBA of nine projects, totaling $2,584,000, with the SBA debenture share at $1,203,000.

The combined number of employees in the nine companies assisted was 368 and they are projecting an increase of 101 to that base because of the 503 activity.

Our news releases received coverage primarily in the rural papers. Some of the bigger newspapers, particularly in the Des Moines area, didn't pick up the story and so the public is just partially aware of the 503 program.

Also, in Iowa, we are continuing in what I would refer to as a recession. There are many layoffs; very few people are spending. I feel with the lack of adequate news coverage we have had and with the recession we are in, we are still showing $1,200,000 in volume. We are now working with SBA. We are going to cover the State with probably, at least, six seminars. We are going to put out news releases and direct mailings to all of our banks and manufacturers.

This effort, along with the possibility of a return to a stronger economy, I feel, is going to substantially increase the volume in 503 activity in our State.

We are projecting probably at least $2 million in debentures to be issued the last half of this year and $5 million next year.

The point I am making here is that we want to be sure that the funding level is adequate. When we get a chance to assist a manufacturer or small business in Iowa to expand and create additional jobs, we want to be sure we are not going to run out of funds, that there will be funds for this program.

Mr. Chairman, I have been asked by staff to comment on another funding level, another program. Should I do that at this time?

Mr. MITCHELL. Sure.

Mr. ALBERTSON. This would be on the SBA 501 program. Under the Small Business Investment Act of 1958, section 501, SBA is authorized to make loans to State development companies for the purpose of assisting eligible small businesses. Twenty-five States have State development companies. Many of these have supplemented their own funds by borrowing from SBA under the 501 program. SBA has informed these development companies there are no longer any direct funds for this program. The SBA loan guarantee authority for development company programs, under sections 501, 502, and 503 has been approved and it was our understanding at $150 million for fiscal year 1983.

The problem is that the 501 development companies under the wording of the Small Business Act of 1958 are eligible for direct loans from SBA, but cannot enter the SBA guarantee program.

The National Association of Business Development Cos., an affiliation of State development companies, requests that this be corrected by amending the Small Business Act of 1958 to give 501 State development companies entrance into the SBA guarantee program.

Thank you, Mr. Chairman.

[Mr. Albertson's prepared statement follows:]

PREPARED STATEMENT OF DON J. ALBERTSON, EXECUTIVE VICE PRESIDENT, IOWA BUSINESS GROWTH CO.

Iowa Business Growth Company made application to SBA for certification under the SBA 503 Program on December 22, 1980, and received certification on May 21, 1981. We were the first statewide 503 company to be certified by SBA.

Upon receiving certification, we completed selection of our Board of Directors and other technical organizational requirements. We furnished news releases to the media; however, we received very limited exposure from this source. We were also on the program at several financing seminars in 1981. Although we reached only a limited number of people through our efforts, we started receiving numerous inquiries and received SBA approval of our first project in August of 1981. With the increased activity of answering inquiries, processing loans, and closing loans, we had little time to continue our efforts to publicize the program.

An additional loan officer was added to my staff in January, 1982. This is allowing us to spend additional time in making a concerted effort to inform a larger portion of the small business and financial institutions in Iowa of the 503 Program. I am presently working with the Des Moines District SBA Office and the Iowa Development Commission in planning a series of meetings in several key locations throughout the State of Iowa. We plan on preceding these meetings with a direct mailing to all financial institutions, local development companies and manufacturers in the State. We feel these efforts will result in multiplying the activities we have thus far experienced.

To date, we have received 320 documented inquiries in regard to the 503 Program. This has resulted in the approval of nine projects totalling $2,584,000 with Iowa Business Growth Company or the SBA 503 Debenture Share at $1,203,000. These nine small businesses had a combined total of 368 employees and project an increase of 101 new jobs as a result of the expansion allowed by this financing. The average size of the nine loans we have approved to date is $150,000, with the largest at $270,000 and the smallest at $54,000.

We feel with the public becoming more aware of the 503 Program and with a return to a stronger economy later this year, we could very likely approve $2,000,000 in loans the second half of this year and $5,000,000 in the following year. In addition to Iowa Business Growth Company, SBA has recently certified six local or city-wide CDC's which will be submitting projects in the near future.

With a current unemployment rate of 6.5 percent, we feel this is an excellent and needed program for assisting small businesses in Iowa. It not only provides financing that is not otherwise available, but at a reasonable maturity and interest rate, not presently available to small business. At the same time, it results in a package that encourages and demands private sector (non-government) participation for at least 50 percent of the project.

Because we feel the State of Iowa and the Nation will benefit from the expansion of small businesses as a result of the 503 Program, we encourage a sufficient funding level to insure that eligible projects will not be turned away due to lack of funds.

Thank you for the opportunity to address you on this subject.

Mr. MITCHELL. Thank you very much.

You have assisted nine companies?

Mr. ALBERTSON. Yes, sir.

Mr. MITCHELL. Could you speculate on what would have been the fate of those companies without your assistance? Would they have maintained status quo or would they have been forced to retrench a little bit or would some of them have gone out of business? Are you able to indicate what would have happened to those companies without the benefit of this program?

Mr. ALBERTSON. Certainly. One case in a very small town was a restaurant that had burned down. Insurance was grossly inadequate to rebuild. We worked with a local development company to provide the funds to rebuild. Now, a restaurant would not normally be a prime candidate under the program. In this case, in a small town, this was the biggest employer in that small town and also, it drew from many miles around that community. It was a very good drawer for that community, drawing people into the trade area. I am sure without 503 assistance in a town that size that they would not have been able to rebuild.

Others would definitely have had to defer expansion, maintain their status quo. Several others very likely could have gone out of existence.

Mr. MITCHELL. Thank you very much.

Congressman McDade.

Mr. MCDADE. Thank you, Mr. Chairman.

Vince, let me ask you a couple of questions, if I may. The chamber has now established through its small business arm a short-term financing mechanism. Since we have had a lot of experience in our community in economic development, how about elaborating a little bit on how that works for the record. Would you?

Mr. MATTEO. On SIDCO?

Mr. MCDADE. Yes. On the $50,000 roughly that is provided to assist these firms with working capital.

Mr. MATTEO. The Scranton Industrial Development Corp., SIDCO, actually was founded in 1915. It was the original industrial development arm of the chamber and now has actually been re-geared and is used for working capital loans to businesses that are in very severe financial situations. We are the lender of last resort. In most instances the businesses which come to us for these loans are on the verge of having their doors locked by banks. The maximum loan is $50,000 for working capital. The term is usually 6 months. We do, at times, expand it to 12 months, and we set an interest rate, the current one is at 15 percent. We usually will accept a first mortgage if that is possible. It usually, of course, is not, and we do like an assignment of contract. And that is usually what the loan is based on. They assign us the contract. All invoices are paid to us. We in turn pay the small business concern so that they can continue to operate and continue to meet the terms of their contracts.

Mr. MCDADE. Vince, what is the source of the $50,000?

Mr. MATTEO. It is private money that was originally raised, I believe, through a number of fund drives, but it is private money from local industry.

Mr. MCDADE. It is the local community response, nontax deductible to the donor.

Mr. MATTEO. Correct.

Mr. MCDADE. To attempt to assist communities. It is in the finest sense of the word a community effort too—because there is no benefit in a selfish manner.

Mr. MATTEO. No, it is a for-profit organization that has never made a profit. Maybe we should loan ourselves the money.

Mr. MCDADE. Maybe we will change that one of these days.

Now, 20 percent of the membership dues, and that is thoroughly commendable—I don't know what the national average would be for the chambers—but in our chamber 20 percent is earmarked for small business efforts.

Mr. MATTEO. That is correct. If I might, Congressman, for instance, a lot of our dues, perhaps, goes to our visitors and convention bureau, which, of course, serves other small businesses. But 20 percent is directly in my program. So, there are even additional funds that aren't counted in that figure.

Mr. MCDADE. Well, how are you going to match this with the 503 program? What is your plan for using that money to leverage 503 additions?

Mr. MATTEO. OK. A lot of that money is committed to other small business activities, in addition, of course, to 503, such as our small business council. We are bringing on a council to assist small businessmen and, of course, we will use some of that fund hopefully for leverage for 503 at a 10-percent local injection. We are also looking to other sources, such as Lackawanna Industrial Fund Enterprise, which is another arm of the chamber and, of course, known as LIFE. So, chamber dues will be used for a number of programs, including the 503 which has the strong commitment of our membership.

Mr. MCDADE. OK. Mr. Albertson, when you went out to assist those companies that you mentioned, what interest rate did you have to go out at?

Mr. ALBERTSON. On the 503 debenture?

Mr. MCDADE. Yes.

Mr. ALBERTSON. It averaged between 14½ and 15½ percent, depending on the closing time.

Mr. MCDADE. Between 14½ and 15½ percent toward—with the exception of the fire disaster you mentioned—expansions or new openings or what?

Mr. ALBERTSON. Each one of the eight others would be expansions.

Mr. MCDADE. They were all expansions. Do you have any idea of the cost per job? I was very impressed with the figures that we heard from Baltimore. What was the cost per job on the 503 program? Do you know?

Mr. ALBERTSON. It is very close to the one job per $15,000 that is now required by SBA's standard operating procedure.

Mr. MCDADE. OK. Larry, under your program you were able to create some jobs at $3,000 per job. That is what I understood your testimony to be, which is really a remarkable figure. Do you want to elaborate on that a little bit and tell me how you were able to leverage it to get it for that, really extraordinary figure?

Mr. SMITH. Well, let's keep in mind that the 503 program is not geared to provide bailout assistance. The 503 program is established to assist firms that have a proven track record and have the ability to manage their businesses properly and continue their growth. This is an assistance program to that end. So, therefore, if we find that we really don't have to overextend the 503 portion, the equity, the infusion is usually adequate to make the deal viable and it is a well-conceived deal initially by the expanding company.

Mr. McDADE. I see. So, you have a strong outfit that you know well. You know their track record and there is an infusion of both equity capital and other types of capital and the 503 leverage is one of the important aspects in the commercial enterprise's ability to expand.

Mr. SMITH. As well as equipment.

Mr. McDADE. Thank you very much.

Mr. SOWER. I might very quickly add, Congressman, that SBA's quarterly report on the 503 program, shows it has been averaging between $3,500 and approximately $5,000 of SBA debenture per job created. So, that is for the national program.

Mr. McDADE. Would you identify the page of that quarterly report?

Mr. SOWER. Page 16 of table 3 of SBA's CDC quarterly review for March 1982, Congressman.

Mr. McDADE. Thank you very much. Thank you, Mr. Chairman.

Mr. MITCHELL. I just have one other question for you, Mr. Smith. Although it is not a major portion of your testimony, you did indicate that a change in the term of the loan would present some problems. I think you said that, didn't you?

Mr. SMITH. Yes.

Mr. MITCHELL. Would you elaborate on that, please?

Mr. SMITH. Actually, it is the increase in the term of the loan. It is a question of exposure. In many cases, the bank, though it would feel comfortable in participating in the project, would want a shorter term, thereby reducing its exposure. The recent amendment to the SOP requires that all participants in the 503 program be in for a minimum of 10 years. So, it is that expansion of the exposure period that is at issue here.

Mr. MITCHELL. Thank you. Gentlemen, thank you very much. I think we are making out a strong case for the positions that the committee has assumed and it is your testimony that enables us to take a very strong position. Thank all of you.

Our next witness is Mr. Martin Cohen who is representing the American Specialty Surety Council. Thank you for being here. I always feel very guilty at these hearings. I know what it means to take almost a whole day away from your operation, and I feel very, very guilty but it is so important that we hear from people who are experts in these various fields, and we thank you very much for being here.

TESTIMONY OF MARTIN COHEN, VICE PRESIDENT, THE AMERICAN SPECIALTY SURETY COUNCIL, ACCOMPANIED BY JOHN MAGNOTTI, EXECUTIVE VICE PRESIDENT, ASSC

Mr. COHEN. Mr. Chairman, my name is Martin Cohen, and I am a vice president of the American Specialty Surety Council. ASSC is an association which unites specialty surety companies, their agents, and that part of the legal community which supports specialty surety firms and agents. With me is John Magnotti, executive vice president of ASSC.

During this past year, the Small Business Administration has taken a series of measures designed to restrict bonding under the surety bond guarantee program below those limits established by

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Congress in the original legislation. Although well meaning, the policy changes in most cases were ill-advised and created a whipsaw action in which neither contractors, specialty sureties, nor agents were quite sure what the rules of the game were at any given moment.

This is not meant to be a criticism of the SBG program managers. Much of the activity in this area has been the direct result of conflicting policy and interpretations at levels higher than program management. However, the net result in the most recent attempt to restrict bonding has been to cause near havoc in the field among contractors who are too small to be bonded by standard sureties and who depend upon bonding guaranteed by the SBA in order to work.

In this most recent effort to reduce bonding levels, SBA limited surety bond guarantees to a maximum of $250,000 and instituted what has been called the 125-percent rule. The rule limited bonds to a maximum amount not more than 25-percent higher than any previously completed construction contract. The result of this action was literally to put many small and minority contractors out of business because of an inability to obtain either bid or completion bonds. Further, the uncertainties and confusion created by this unfortunate policy statement have caused what might be permanent damage to the program and a loss of confidence in the Government by both the surety industry and small and minority contractors.

During the most recent hearings on this program in the Senate, it was implied by the chairman of the Small Business Committee that much of the confusion in policy emanating from the SBA is due to a failure to involve the surety industry in the decisionmaking process, at least to provide comments on draft policy and operation documents. I would like to emphasize this point, Mr. Chairman. I am a small businessman operating a successful surety company, and my experience is gained as a result of thousands of decisions made daily in providing bonding for hundreds of small and minority contractors in the State of Tennessee. My experience is duplicated by my many colleagues who work in surety firms or act as agents or legal counsel in the surety area.

I feel that our advice can be used by the SBA in evaluating policy proposals and operating documents. We have made specific requests to the SBA on several occasions that we be permitted to comment on policy statements prior to publication. At times we have been permitted limited participation, but in the most recent case, we were completely closed out until that unfortunate policy was announced. As I stated before, the effect was devastating. Not only were surety companies, agents, and contractors confused and hurt financially, but the reaction by SBA officials in the field was equally uncertain and confused.

As a result of the actions taken so far in the program, we strongly support the legislation proposed in H.R. 6086 to expressly prohibit the SBA from limiting the maximum amount of a bond below the statutory limit and from utilizing a percentage increase limitation except on a case-by-case basis. It has been noted that the SBA eliminated most of the problem by rescinding their latest restrictive policy on April 1 of this year. However, the management of

the program has been so erratic thus far and so many changes have been promulgated so rapidly that we must agree that positive measures must be taken to guarantee that another devastating policy change is not announced without notice. Legislation to ensure that congressional policy is followed appears to be an absolute necessity if this program is to survive and if the bonding community is to be able to establish long-range working policies and procedures to assist small and minority businessmen in their efforts to enter the contruction business.

Although not currently mentioned in the legislation, we would like to make one additional suggestion which will materially assist the program. An alternative solution to the guarantee budget problem is to permit guarantees from successfully completed contracts to be recycled into the system and made available for additional bonding.

It must be remembered that the guarantee programs are just that: Guarantees. Federal moneys are not being expended, except in defaults, and the Federal Government is merely extending its credit in a proper manner to assist small and minority businessmen in the formative stages of their businesses when they are unable to provide sufficient credit in order to obtain necessary bonding.

It appears to be logical that guarantee levels can and should be recycled as contracts are completed successfully. This policy, coupled with the policy currently included in H.R. 6086 will provide a solid basis upon which the entire bonding community can build an effective program for assisting small and minority contractors.

In summary, Mr. Chairman, we are pleased to have been asked to testify at these hearings. We recommend strongly that the provisions now in H.R. 6086 be included in the final legislation and that in addition action be taken to permit recycling of guarantee levels as bonds are successfully completed.

My colleague and I are prepared to answer any questions that you or the committee might have.

Thank you.

Mr. MITCHELL. Thank you. You thanked us for hearing you, but just based on that one recommendation which I think is very, very significant, I mentioned to the staff that we need to pursue this.

Mr. COHEN. Well, Mr. Congressman, for many years I've been in the program, since the inception of the program in 1971, before there even was a program that got off the ground. Actually, over the years, I've made mention of this numerous times. Of course, SBA became much more sophisticated with the program and it has grown.

In other words, just to show the magnitude of the program, how it has grown, it is probably the second largest program at the Small Business Administration. In other words, the loan program began in 1945 originally, and it's been in effect approximately 32 years. It has about 800 people participating nationwide. The bond program, begun in 1971, only 11 years ago, has 56 people actually participating in the program at the SBA nationwide. SBA has guaranteed about 300,000 contracts which represent a little over $18 billion worth of individual contracts.

As far as the amount of claims, actually only about $156 million has been paid out in 11 years. This is a very infinitesimal amount when you talk about $18 billion worth of individual contracts.

To put things in the proper perspective, if you take a look at the difference between the winning bid and the second low bidder, you would find somewhere between 3- and 5-percent savings on the amount of the bids.

So the program actually is making money for the taxpayer, not costing the taxpayers any money.

Mr. MITCHELL. Thank you. I'd just like to comment that this has been the biggest headache for me since I've been in the Congress: The bonding problem. And like you, I was simply aghast at the recommendations that came from SBA last year. It simply didn't make sense to take that kind of approach, and I am very pleased that the committee wielded significant pressure to at least get them to examine the issue on a case-by-case basis. That's not the best solution but it was far better than what had been proposed by the SBA under its previous Administrator.

I agree that we certainly need your expertise and I, for one, may have to commit myself that from time to time, I'll be calling on you when we have more problems with the bonding issue. If SBA doesn't want to avail itself of your expertise, certainly, this committee does.

Mr. COHEN. I appreciate it. A lot of people have a misconception, Congressman, of what the bonding issue is all about. Basically, the bonding business is like seed money going into a project. Every Federal, every State, every municipal job in the country over, say, $50,000 requires a performance bond.

Without that piece of paper, nothing else starts. It backs up all the way. You know, the banks, savings and loans, drug stores, all the way down the line. So numerically, in terms of people employed, you're talking about probably millions that it affects.

Mr. MITCHELL. Mr. Hiler?

Mr. HILER. Thank you, Mr. Chairman. Mr. Cohen, how many surety bonds do you issue a year?

Mr. COHEN. How many do we in Tennessee, sir? We issue about 250 to 350 a year in Tennessee.

Mr. HILER. 250 to 300?

Mr. COHEN. Correct.

Mr. HILER. What is the range—I'm not talking about SBA guaranteed, just total surety bond.

Mr. COHEN. Total surety bonds—I'd say about half are SBA guaranteed bonds, sir.

Mr. HILER. About half are SBA. And what is the range of those surety bonds that you issue?

Mr. COHEN. The average bond we issue is somewhere between $250,000 and $400,000.

Mr. HILER. $250,000 and $400,000 is the average. Who are the people who come before you? Just describe who the people are that come before you that are not an SBA company, who have an SBA guarantee, and who are the companies that come before you that need the SBA guarantee?

Mr. COHEN. Let me differentiate. Basically, we are a specialty association. In other words, if someone can normally stand on their

own two feet and does not need some other financial assistance, they are the ones that are not going to participate in the SBA bond program. Those that need SBA's guarantee are people that need financial assistance, that have not been in the contracting business over 3 or 4 years. If a contractor hasn't been in business for 3 to 5 years, most of your standard companies won't help no matter what your statements show. Just because you have dollars, per se, does not necessarily mean that you have the expertise to complete jobs.

Mr. HILER. Now, when did you issue your first SBA guaranteed surety bond?

Mr. COHEN. I've been in the program since the inception in 1971. The exact date—I'm not 100 percent sure but it was probably somewhere in 1971, sir.

Mr. HILER. 1971? Do you have any of the same firms that were issued surety bonds under the guarantee in 1971 that are now getting them from you without the guarantee?

Mr. COHEN. If you are asking me if we have graduated a great deal, we've graduated a few, not a great deal.

Mr. HILER. You have not graduated a great deal?

Mr. COHEN. No, sir.

Mr. HILER. So, now, is that because those firms no longer come before you or because they continue not to be financially solvent enough to go without the guarantee program?

Mr. COHEN. Both, sir. A lot of them actually have not grown to the point where the standard surety market will let them participate, and a lot of them did not make it financially, sir.

Mr. HILER. What percent of your revenue comes from the SBA-guaranteed section?

Mr. COHEN. We're a small company in Tennessee. Approximately 15 percent of our total gross volume of business written is within the bond program. Now, if you ask me as far as SBA, probably about 8 or 9 percent, sir.

Mr. HILER. Eight or nine percent.

Mr. COHEN. Correct, sir.

Mr. HILER. You had mentioned, in response to some questions from the chairman, that you felt that the guarantees were a good idea and that, in fact, they could be recycled so that they continually expand. Why doesn't the Government just guarantee every bond that's out there?

Mr. COHEN. I'm not quite sure. You say guarantee every bond?

Mr. HILER. Guarantee every surety bond.

Mr. COHEN. By every contractor in the country?

Mr. HILER. Sure.

Mr. COHEN. Then I think there would be no requirement in underwriting whatsoever as far as trying to underwrite the contract to make it a successful contract—it would be just carte blanche.

Mr. HILER. I guess my point is because you said it makes the Government money, and right now, the Government is looking for money, so just by giving more guarantees, we can make more money. It would seem like that would be a thing to do. I guess my point is that I think we have to be concerned about priorities and about setting levels. I think we have to set some type of level. So when you recycle, when you just allow that to continually build, build, build—or would you set some type of level there?

Mr. COHEN. Well, in other words, when I talk about recycle, once a contract has been completed successfully and all the bills are paid and that's documented, that contract value would go back into the system. As far as setting a definite limit on total amount, whatever the numbers are, that could be done taking into consideration inflation.

I'd say you'd have to take into consideration the time and put everything in the proper perspective.

Mr. HILER. So that you would envision, then, that what we would do would be to add to the pool every year from appropriations here in the Congress and then everything that had been appropriated or authorized in the past would continue to expand. Is that how you anticipate it working?

Mr. COHEN. Basically, I think what we are talking about is having a level of $1.5 billion or $1.6 billion and leaving that permanently and just letting the program take care of itself on a recycling basis. I think that would more than adequately handle the situation.

Mr. HILER. At what level did you say?

Mr. COHEN. About $1.5 billion or $1.6 billion.

Mr. MAGNOTTI. The Congress has authorized, I believe, $1.4 billion at this time; that is, $1.2 billion for the House and $1.6 billion for the Senate. But if you leave it at that level, let whatever can be recycled be recycled. The market forces are going to take care of a lot of it.

Mr. HILER. No further questions, Mr. Chairman. Thank you very much. I appreciate it.

Mr. MITCHELL. Thank you, gentlemen, very, very much. We are going to explore this business of recycling because I think it makes eminent good sense.

Mr. COHEN. Thank you.

Mr. MITCHELL. Thank you very much. Before hearing from our next panel, let me warn my opponents on Capital Hill. Three of our witnesses earlier this morning were from the city of Baltimore. They have departed. However, other troops have arrived. These are the Northwestern Senior High School ninth graders, who are in the room now, and we are just delighted that you would visit with us today. The teacher is Mrs. Mary Oather, right?

We are delighted that you can visit this hearing with us and visit Washington, and I feel much more comfortable. When you leave, I hope another contingent from Baltimore will come in so that my security blanket is maintained very closely around me.

Thank you very much for visiting us.

Our next panel is Mr. Herman Director, representing the National Small Business Association; Mr. Ronald Peterson, representing the National Tooling & Machining Association; and Mr. William Creager, representing the National Association of Small Government Contractors.

Gentlemen, thank you very much. Congressman Addabbo was here. He assured us that we would benefit singularly by your testimony. He has had to go to the Appropriations Committee for further work, so we thank you.

Why don't we lead off with Mr. Director, and then Mr. Peterson and then Mr. Creager.

PANEL CONSISTING OF HERMAN DIRECTOR, RONALD PETERSON, AND WILLIAM CREAGER

TESTIMONY OF HERMAN DIRECTOR, REPRESENTING THE NATIONAL SMALL BUSINESS ASSOCIATION

Mr. DIRECTOR. Thank you very much, sir. My name is Herman Director, and I am the chief economist for the National Small Business Association, a multi-industry trade association representing approximately 50,000 small business firms nationwide. We wholeheartedly support H.R. 5551, a bill that would improve small business access to Federal procurement information.

It has been a long-standing policy of our Government to rely on competitive private bids for goods and services. Recent figures, however, indicate that there is room for improvement in small business participation in Government procurement. As a service to our members, we, at NSB, operate a nationwide service known as bidders early alert service—BEAM—which notifies members of sales opportunities to Government using the Commerce Business Daily. Members file with NSB a list of the products and services they offer for sale. BEAM matches Government bid requests with this listing and notifies the participating member immediately.

This system has been in operation for 11 years during which time over 29,000 BEAM notices have been issued. Our experience indicates that there are many obstacles to small business participation in Government procurement. Foremost among these are: Inadequate time allowed from the date of publication of the bid notice in the Commerce Business Daily to the bid opening date; and inadequate time allowed from the date of publication of the bid notice in the Commerce Business Daily to closing date for honoring requests for bid sets.

The U.S. Department of Commerce is responsible for compiling, editing, and publishing the Commerce Business Daily. We've had meetings and discussions with responsible officials of the Department of Commerce directed toward improvement in the CBD which would facilitate its use by small business.

We've been assured by the Department of Commerce that consideration will be given to our suggestions. Changes in procedure suggested include the extension of time for solicitation and bidding as recommended in H.R. 5551. We also suggest that the CBD format be modified to list bid opportunities and specific categories as follows: Competitive bids, (a) open and, (b) small business set-asides; information synopses for subcontractors alert; noncompetitive notice listings; contract awards listings for both (a) open, and (b) small business set-asides.

We also suggest that consideration be given for listing bid opportunities by four digit SIC code identification. This would permit a more direct identification of products and services of interest to potential bidders and provide a more readily identifiable basis for assessing business participation in the Government procurement market, by types of business in relation to the Government procuring agency area of specific interest. A suggested format is included.

As an indicator of the current CBD listings of bid opportunities allowing 10 days or less for response, attached is a selected list of bid notices from the CBD issued March 4, 1982. Our experience

over the past 10 years with the NSB BEAM service which alerts our members to Federal requests for bids indicates that many opportunities for small business are lost due to the inadequate time allowed for receiving bid notices and preparation of bids. We therefore support H.R. 5551 which extends the time for requesting bid papers, and preparing bid proposals on Government procurement opportunities.

Thank you very much.

Mr. MITCHELL. Thank you, sir. I'd like to suggest that we proceed by hearing from all three of the witnesses, and then we will raise questions.

Without objection, Mr. Director, the attachments to your statement will be inserted into the record.

[The attachments to Mr. Director's statement follow:]

Suggested Format CBD

ATTACHMENT I

CODE	PRODUCT SERVICE DESCRIPTION	SPECIFICATIONS FSN	MIL	P/N	QUANTITIES	DESTINATIONS	REQUEST BID PAPERS BY ID FROM AGENCY AS LISTED	BID DUE DATE	FOR INFO CALL	SEE NOTE

ATTACHMENT II

SELECTED BID NOTICES

COMMERCE BUSINESS DAILY, MARCH 4, 1982

(Product Service -- Bid Due Date -- Procuring Agency)

Small Office Building Design Team -- March 13, 1982 -- Battelle Northwest.

Bibliographic Data Retrieval Services -- March 8, 1982 -- Acquisition Division US Army Medical R&D Command.

Financial Advisory Services -- March 8, 1982 -- Commander, Military Sealift Command.

Removal, Overhaul, Repair and Reinstall Detroit Diesel 4-53 Engines -- March 11, 1982 -Contracting Officer.

Sludge Removal from Oil/Water Separators -- March 2, 1982, Contracting Office, Fort Lewis.

Bearing -- March 3, 1982 -- Defense Industrial Supply Center.

Electronic Unit -- March 11, 1982 -- Contracting Division, Fort Hood.

Variable Transformer -- March 8, 1982 -- Defense Electronics Supply Center.

Relay, Dropout -- March 11, 1982 -- Defense Electronics Supply Center.

Relay Armature -- March 10, 1982 -- Defense Electronics Supply Center.

Electron Tube -- March 5, 1982 -- Defense Electronics Supply Center.

Electron Tubes -- Feb. 25, 1982 -- Defense Electronics Supply Center.

Electron Tube -- March 5, 1982 -- Defense Electronics Supply Center.

Electron Tubes -- March 4, 1982 -- Defense Electronics Supply Center.

Connector, Plug -- March 5, 1982 -- Defense Electronics Supply Center.

Type IIC Modification Kits -- March 11, 1982 -- FAA, Mike Monroney Aeronautical Center.

Upgrade of Existing Audio-Visual System -- March 4, 1982 -- U.S. Army Engineer District San Francisco.

Pipet, Serological, Plastic, Disposable -- March 11, 1982 -- Defense Personnel Support Center.

Circuit Card -- March 11, 1982 -- Navy Ships Parts Control Center.

Chemical Metering -- March 5, 1982 -- Tennessee Valley Authority.

Environmental Test Chambers -- March 9, 1982 -- Regional Contracting Dept.

Software Information for Communication Network Optimization -- March 10, 1982 -- Headquarters Air Force Communications Command.

This is a Notice of Intention to Procure from the GSA ADP Schedule -- March 8, 1982 -- Wright-Patterson AFB.

Mr. MITCHELL. Mr. Peterson, welcome. A double welcome; I'm doing it for myself, and for Congressman Addabbo.

TESTIMONY OF RONALD A. PETERSON, REPRESENTING THE NATIONAL TOOLING & MACHINING ASSOCIATION

Mr. PETERSON. Thank you, Mr. Chairman. I would like to submit a copy of my testimony for the record and speak informally, if I may.

Mr. MITCHELL. Without objection, your statement will appear in its entirety in the record.

Mr. PETERSON. Thank you.

[The prepared statement and attachments of Mr. Peterson follow:]

PREPARED STATEMENT OF RONALD A. PETERSON, REPRESENTING THE NATIONAL TOOLING & MACHINING ASSOCIATION

MY NAME IS RONALD A. PETERSON. I AM A SMALL BUSINESS MAN EMPLOYED AS VICE-PRESIDENT & ECONOMIST OF PITKIN MANUFACTURING INC., A SMALL MANUFACTURING FIRM IN BROOKLYN NEW YORK, WHICH IS OWNED BY MY FAMILY. I AM ALSO PRESIDENT OF THE NEW YORK CHAPTER OF THE NATIONAL TOOLING AND MACHINING ASSOCIATION, AN ASSOCIATION OF COMPANIES ENGAGED IN CONTRACT WORK. THE MEMBERSHIP OF THE ASSOCIATION TOTALS MORE THAN 4000 MEMBER COMPANIES NATIONWIDE.

I VERY MUCH APPRECIATE THE COMMITTEE'S INVITATION TO TESTIFY TODAY. THIS IS A MATTER THAT CONCERNS OUR ASSOCIATION INCLUDING MY FIRM IN A VERY DIRECT MANNER. THE COMMERCE BUSINESS DAILY IS OUR SOLE SOURCE OF INFORMATION ENABLING US TO MONITOR GOVERNMENT CONTRACTING OPPORTUNITIES. THE REASON FOR THIS IS SIMPLE , THE MAJORITY OF SMALL BUSINESSES ARE UNDERCAPITALIZED. THEREFORE, SMALL BUSINESS IS OPERATING UNDER A FINANCIAL CONSTRAINT WHEREBY SALES REPRESENTATIVES AT ANY PROCURING ACTIVITY, LET ALONE WASHINGTON D.C., ARE SIMPLY UNAFFORDABLE.

SPECIFICALLY, MY OWN EXPERIENCE IN DEALING WITH THE COMMERCE BUSINESS DAILY BEGAN SEVEN YEARS AGO IN 1975. DURING THE '74-'75 RECESSION, PITKIN MFG. LOST A MAJOR SOURCE OF BUSINESS. AN INDUSTRY

GROUP, WHICH ACCOUNTED FOR APPROXIMATELY 50% OF OUR SALES, STARTED IMPORTING THEIR MACHINE PART REQUIREMENTS FROM TAIWAN IN AN ATTEMPT TO CUT COSTS. IN SEARCH OF A RECESSION PROOF INDUSTRY AS A CUSTOMER WE DIRECTED OUR EFFORTS TOWARD GOVERNMENT CONTRACT OPPORTUNITIES. OPERATING WITHIN THE FINANCIAL CONSTRAINT, OF BEING UNDER CAPITALIZED, THE COMMERCE BUSINESS DAILY BECAME OUR SOLE SOURCE OF INFORMATION. I HAVE BEEN READING THIS PUBLICATION FOR THE PAST SEVEN YEARS ON A DAILY BASIS. I MIGHT ADD THAT GOVERNMENT CONTRACTS ACCOUNTED FOR 90% OF OUR SALES IN 1981.

SPEAKING FOR ALL THE MEMBERS OF THE NATIONAL TOOLING AND MACHINING ASSOCIATION AND MYSELF, I AM IN FULL SUPPORT OF THIS LEGISLATION (HR5551). TWO MAJOR PROBLEMS WITH THE COMMERCE BUSINESS DAILY ARE THE TIME FRAME AND INCORRECT CLASSIFICATION OF PROCUREMENT NOTICES. FREQUENTLY A SYNOPSIS APPEARS EITHER TOO LATE TO PERMIT THE SUBMISSION OF A TIMELY AND AN INTELLIGENT BID OR IT APPEARS UNDER A WRONG CLASSIFICATION.

IT IS RARE THAT A SYNOPSIS IS PUBLISHED TEN DAYS BEFORE A SOLICITATION IS ISSUED. FURTHERMORE, IT IS NOT UNCOMMON FOR A PROCUREMENT NOTICE TO FIRST APPEAR ONLY TWENTY DAYS BEFORE THE SOLICITATION'S OPENING DATE. (RECENT EXAMPLES ARE ATTACHED)

A FACTOR WHICH MUST NOT BE OVERLOOKED IS WHAT I REFER TO AS THE "POSTAL PERIOD". THAT IS TO SAY, THE TOTAL LENGTH OF TIME BIDDING DATA IS IN THE HANDS OF THE POSTAL SERVICE. THIS PERIOD CONSISTS OF FOUR SEPARATE TIME SEGMENTS, DURING THE USUAL COURSE OF THE BIDDING CYCLE. THESE FOUR TIME SEGMENTS ARE:

1. THE NUMBER OF DAYS ELAPSED FROM THE PUBLISHED DATE OF THE CBD UNTIL THE ACTUAL DATE THE SUBSCRIBER RECEIVES IT. IT IS NOT UNCOMMON

TO RECEIVE IT FIVE DAYS AFTER THE PUBLISHED DATE.

2. THE NUMBER OF DAYS IT TAKES FOR A REQUEST, MAILED BY THE CONTRACTOR TO ARRIVE AT THE PROCURING ACTIVITY.

3. THE NUMBER OF DAYS IT TAKES FOR THE CONTRACTOR TO RECEIVE A COPY OF THE SOLICITATION WHICH IS BEING REQUESTED, AFTER THE PROCURING ACTIVITY RECEIVES THE REQUEST. THIS PERIOD INCLUDES TIME FOR PROCESSING THE REQUEST, AND TIME IN THE MAIL. ALTHOUGH (2) AND (3) CAN BE COMBINED THE COMBINATION OF THE TWO WILL NOT PROPERLY ACCOUNT FOR TWO TIMES THE DATA IS IN POSTAL HANDS.

4. THE NUMBER OF DAYS THE CONTRACTOR MUST MAIL ITS BID OR PROPOSAL BEFORE THE OPENING DATE. PROCUREMENT ACTIVITIES REQUEST BIDDERS TO MAIL THEIR BIDS FIVE DAYS BEFORE THE OPENING DATE IN ORDER TO INSURE TIMELY RECEIPT OF THE BIDS.

EACH ONE OF THE FOUR TIME SEGMENTS LISTED ABOVE CAN EASILY TAKE FIVE DAYS. THEREFORE, IF A SOLICITATION IS OPENING TWENTY DAYS AFTER AFTER THE BIDDER RECEIVES THE COMMERCE BUSINESS DAILY, THE BIDDER MAY ONLY HAVE FIVE DAYS INORDER TO PREPARE THE BID. IN THE CASE OF MANUFACTURERS THIS IS SIMPLY NOT ENOUGH TIME TO SUBMIT A TIMELY AND AN INTELLIGENT BID.

I ADDRESS THE MANUFACTURER'S POINT OF VIEW SPECIFICALLY BECAUSE OF MY POSITION IN THE ASSOCIATION AND THE NATURE OF MY BUSINESS. A MANUFACTURER FACES MANY TIME CONSUMING TASKS IN THE BIDDING PROCESS THAT A REGULAR DEALER OR DISTRIBUTOR DOESN'T ENCOUNTER. FOR EXAMPLE, AN ITEM THAT PITKIN MFG. HAS MANUFACTURED UNDER CONTRACT FOR THE DEPARTMENT OF THE ARMY IS A BIPOD ASSEMBLY: M3. IN ORDER TO SUBMIT AN INTELLIGENT AND A RESPONSIBLE BID ON THIS ITEM A BIDDER WOULD NEED PRICE AND DELIVERY QUOTES FROM THEIR SUPPLIERS. IN HOPES OF SUBMITTING

THE LOW BID, THE BIDDER MUST TRY TO OBTAIN AT LEAST THREE QUOTES FROM DIFFERENT SUPPLIERS FOR EACH PART IN THE ASSEMBLY. IN ADDITION THE BIDDER MUST ALSO ESTIMATE TOOLING AND PRODUCTION TIME AND COSTS.

THE BIPOD ASSEMBLY RESEMBLES A GIANT CLOTHES PIN AND DOESN'T APPEAR TO HAVE MANY PARTS IN THE ASSEMBLY. YET, IN ORDER TO PROPERLY SUBMIT A BID FOR THIS ITEM A BIDDER WOULD NEED TO HAVE AT LEAST THREE QUOTES FOR EACH OF THE FOLLOWING ITEMS:

1. STEEL TO FABRICATE THE LEGS AND STIFFENERS
2. PIVOT PINS FROM A SCREW MACHINE HOUSE
3. STEEL WASHERS FROM A SUPPLY HOUSE
4. SPRINGS FROM A SPRING MANUFACTURER
5. HEAT TREATING FROM A METAL FINISHER
6. PHOSPHATE COATING FROM A METAL TREATER
7. PLASTIC BAGS AND BOXES FOR PACKAGING

IN ADDITION TO THIS A BIDDER MUST ALSO ESTIMATE:

8. TOOLING TIME AND COST
9. PRODUCTION TIME AND COSTS, NOT TO MENTION METHODS

KEEP IN MIND, DUE TO THE FACTOR WHICH I LABELED THE "POSTAL PERIOD" THE BIDDER MAY ONLY HAVE FIVE DAYS TO ACCUMULATE, CORRELATE AND EVALUATE ALL THIS INFORMATION IN ORDER TO SUBMIT A TIMELY BID. CLEARLY, TO DO ALL THIS PROPERLY WOULD TAKE MORE THAN FIVE DAYS. IN ADDITION TO ALL THIS WORK , IF THE BIDDER NEEDS A COPY OF A SPECIFICATION NOT IN HIS FILE THE BIDDER MUST MAIL AWAY TO THE NAVAL FORMS PUBLICATION CENTER IN PHILADELPHIA P.A.. THIS TIME DELAY FOR SURE WILL NOT ALLOW THE BIDDER SUFFICIENT TIME TO SUBMIT THE BID.

YOU MAY ASK, IF THIS IS THE CASE HOW DOES ANY BIDDER SUBMIT A TIMELY BID? THE ANSWER TO THAT QUESTION, IS SOMETHING CALLED "LOW BALLING" LOW BALLING IS A PRACTICE WHICH IS NOT UNCOMMON. THE WAY ONE WOULD LOW BALL A BID IS BY BIDDING LESS THAN THE PREVIOUS PRICE PAID BY THE

GOVERNMENT FOR THAT ITEM. IN THE LONG RUN, THIS PRACTICE ONLY LEADS THE CONTRACTOR DOWN ONE PATH, TOWARD FINANCIAL DESTRUCTION. THE GOVERNMENT IS ALSO HURT BY THIS PRACTICE. IT MAY "CROWD" OUT GOOD CONTRACTORS FROM THE SYSTEM AND SERIOUSLY DELAY NEEDED REQUIREMENTS. THEREFORE, UNDER THE CURRENT BIDDING CLIMATE WHICH HAS BEEN PRECIPITATED BY THE TIME FRAME PRESENT IN THE COMMERCE BUSINESS DAILY A GOOD, QUALIFIED , METICULOUS CONTRACTOR HAS MORE TO LOSE THAN TO GAIN BY GETTING INVOLVED IN GOVERNMENT BIDDING.

THE POTENTIAL BUSINESS LOST DUE TO THE CURRENT PROBLEMS WITH THE COMMERCE BUSINESS DAILY IS HARD TO ESTIMATE. IF A SYNOPSIS APPEARS UNDER A WRONG CLASSIFICATION THERE IS A GOOD CHANCE THE POTENTIAL CONTRACTOR WILL NEVER SEE IT. THEREFORE, POTENTIAL BUSINESS LOST DUE TO AN "IMPROPER" NOTICE IS VERY HARD TO ESTIMATE. HOWEVER, I WOULD ESTIMATE THAT MY FIRM ALONE LOST APPROXIMATELY $500,000.00 WORTH OF POTENTIAL BUSINESS DUE TO TIME CONSTRAINTS IN BIDDING. THIS VERY CONSERVATIVE ESTIMATE DOES NOT INCLUDE THE COUNTLESS NUMBER OF SOLICITATION SETS THAT WE NEVER RECEIVED. THE PROCUREMENT ACTIVITY USUALLY MAILS A FORM NOTICE THAT EXPLAINS THEIR SUPPLY OF SOLICITATION SETS IS EXHAUSTED. (SEE ATTACHED LETTER) THIS PROBLEM IS A DIRECT EFFECT OF THE TIME CONSTRAINT CURRENTLY PRESENT IN THE COMMERCE BUSINESS DAILY .

I BELIEVE THAT THE REQUIREMENTS OF THIS LEGISLATION (HR5551) WILL HELP ELIMINATE THE PROBLEMS THAT CONFRONT MANY SMALL BUSINESSES AS I HAVE OUTLINED ABOVE. THE STIPULATIONS THAT PROPER NOTIFICATION BE PUBLISHED AT LEAST FIFTEEN DAYS BEFORE ISSUANCE OF A SOLICITATION AND THEN AT LEAST THIRTY DAYS MUST ELAPSE BEFORE COMPETITION CAN

BE CLOSED, WILL PROVE TO BE ONE OF THE MOST IMPORTANT FACTORS BENEFITING SMALL PRIME CONTRACTORS IN THE FUTURE.

IN CONCLUSION, I WOULD LIKE TO ADD THAT THIS LEGISLATION IS IN THE BEST INTERESTS OF BOTH THE GOVERNMENT AND SMALL BUSINESS. THE GOVERNMENT WILL ENJOY THE BENEFITS FROM INCREASED COMPETITION WITH THE SIDE EFFECT OF INCREASING THE DEFENSE INDUSTRIAL BASE. SMALL BUSINESS WILL ENJOY AN INCREASE IN CONTRACT OPPORTUNITITES. I BELIEVE THIS IS ONE OF THOSE SITUATIONS WHERE EVERYONE INVOLVED CAN COME OUT A WINNER. I WOULD LIKE TO ADD THREE WAYS, I SEE, OF IMPROVING THE CURRENT PROCUREMENT SYSTEM:

1. BY MAKING THE COMMERCE BUSINESS DAILY AVAILABLE ON A "SAME DAY" BASIS VIA AN ON-LINE DATA BASE
2. PROVIDING ALL NEEDED SPECIFICATIONS WITH THE BID SET
3. BY SIMPLIFING THE SOLICITATION IN GENERAL

I HAVE CONFINED MY STATEMENT TO THE ISSUE IN FRONT OF THE COMMITTEE TODAY. HOWEVER, IF YOU WOULD LIKE TO DISCUSS THE POSSIBILITIES I HAVE OUTLINED OF IMPROVING THE PROCUREMENT SYSTEM PLEASE FEEL FREE TO CALL ON ME.

THANK YOU FOR THE INVITATION TO TESTIFY TODAY AND IF YOU HAVE ANY QUESTIONS I WOULD BE HAPPY TO ANSWER THEM.

# # #

BEST COPY AVAILABLE

91--CORRECTION: JACK, PUSH-PULL SCREW; McMaster Carr Part No. 2[illegible] or equal. IFB DTCO40-82-B-40049. Bid opening to be 2/5/82 in lieu of 1/22/82. Correction to PSA-7[illegible] dated December 31, 1981. (011)
U.S. Coast Guard Yard, Curtis Bay, Baltimore, MD 21226, Attn: Contracting Officer

91--TOOL KIT, RIVETER, Consisting of a hydraulic hand riveter and accessories - Std No MFR-E-MARS21-ES-F to be issued o/a March 22, 1982. Quantity, 89 - Unit of Issue, KT - FOB, Orinda, Firms interested in bidding should submit their request for a bid set in writing before Feb. 22, 1982. (012)
GSA, FSS, Contracts Div. 9FCB-ES (Mary Parks), 1500 E. Bannister Road, Kansas City, MO 64131

91--STUD REMOVER & SETTER - Fed Spec GGG-S-775a dtd 6-8-60 & Amend. 2 dtd 1-11-65 - Size, Various - Quantity, 29 - Unit, SE - FOB Points, CONUS - RFQ MFR-S-MARS7-ES-I--Opening date, COB 2-4-82. (012)
GSA, Region 6, Business Service Center, 1500 E. Bannister Road, Kansas City, MO 64131

91--CORRECTION: PSA-7[illegible] 21 Dec 81. Jack, Push-pull screw; McMaster Carr part no. 2[illegible] or equal. IFB DTCO40-82-B-42048. Bid opening date to be 2 Feb 82 in lieu of 22 Jan 82. (012)
U.S. Coast Guard Yard, Curtis Bay, Baltimore, MD 21226 Attn: Contracting Officer

52 Measuring Tools.

52--MEASURING TOOLS--30 items, various quantities--deliver to Pearl Harbor, HI--N00604-82-B-A110--Approx opening 27 Jan 82. Request for copies of solicitation must be received NLT 10 days prior to opening date. (012)
Commander (SCD), Pearl Harbor Naval Shipyard, Box 400, Pearl Harbor, HI 96860, Helen Fowler 808/423-1501

53 Hardware and Abrasives.

53--BOLT MACHINE NSN 5306-00-114-2539--Spec Goodyear P/N 9192-65--4830 ea--QPL--Deliveries to DCSC Columbus OH; Def Dep Memphis, TN--RFP DLA600-82-R-0887--RFP due date 11 Feb 82--For tech info G. Keyserman, 215/697-3247--See notes 73 and 55.

53--PIN RIVET NSN 5320-00-916-4773--Spec MAS 1466-05--360,000 ea--Deliveries to DCSC Columbus, OH--S/O DLA600-82-S-1476--Bid opening date 11 Feb 82--For tech info E. McCleary, 215/697-4220--See notes 4 and 55.

53--SEAL, MECHANICAL, ASSEMBLY NSN 5331-00-451-5215--Spec Dimer Corp, P/N 305 135--155 ea--Deliveries to NSC Norfolk VA; NSC Oakland CA; Def Dep Ogden, UT--RFP DLA600-82-R-0024--RFP due date 11 Feb 82--For tech info J. Creeden, 215/697-3435--See notes 73 and 55.

53--SEAL, PLAIN ENCASED NSN 5330-00-143-5996--Spec DWG 7921241 REV E A/19/67, DWG 7921241, REV G 2/22/66--21,500 ea--Deliveries to Army Depot New Cumberland PA; Def Dep Ogden, UT--S/O DLA600-82-S-1473--Bid opening date 11 Feb 82--For tech info J. Rudisill, 215/697-3284--See notes 4 and 55.

53--PACKING MATERIAL, GRAPHITE GRANDED YARN NSN 5330-01-230-9210--Spec VAV SPEC NR DOD-P-24805 (SH) dtd 76 Mar 08--400 Lb--Deliveries to NSC Norfolk, VA; NSC Oakland, CA; Def Dep Ogden, UT--S/O DLA600-82-S-1472--Bid opening date 11 Feb 82--For tech info E. Williams 215/697-3242--See notes 4 and 55.

53--WASHER, CONVEX NSN 5310-00-733-0980--Spec Worthington Pump Co. P/N BK167921--400 ea--Deliveries to various destinations--RFP DLA600-82-R-0576--RFP due date 10 Feb 82--For tech info S. Shultz, 215/697-3410--See Notes 73 and 55.

53--NUT, EXTERNAL WASHER, DOUBLE HEXAGON NSN 5310-00-680-7342--Spec GMC P/N 9736290-044--14,000 ea--Deliveries to Def Dep Memphis, TN--RFP DLA600-82-R-0574--RFP due date 10 Feb 82--For tech info S. Shultz, 215/697-3410--See notes 73 and 55.

53--NUT SELF LOCKING BARREL NSN 5310-00-489-0699--Spec Amerace/Esna P/N 2882-144--1200 ea--Deliveries to Def Dep Memphis, TN; Def Dep Ogden, UT--RFP DLA600-82-R-0573--RFP due date 10 Feb 82--For tech info W. Cox, 215/697-3427--See notes 73 and 55.

53--NUT, PLAIN ROUND NSN 5310-00-080-3427--Spec. P/N 36745 Chandler Evans--1600 ea--Deliveries to def Dep Memphis, TN; Def Dep Ogden, UT--RFP DLA600-82-R-0575--RFP due date 10 Feb 82--For tech info S. Shultz, 215/697-3410--See notes 73 and 55.

53--CASTER, SWIVEL, NSN 5340-00-995-0391--Spec MW Aerol Co. Los Angeles CA P/N 913-1-0-SR12--240 ea--Deliveries to Def Dep Memphis, TN--RFP DLA600-82-R-0577--RFP due date 10 Feb 82--For tech info J. Cuccolo, 215/697-3427--See notes 73 and 55. (012)
Defense Industrial Supply Center, 700 Robbins Ave., Philadelphia, PA 19111, Tel 215/697-3668

53--BOLT, MACHINE--NSN 5306-00-825-7963--Spec Firestone Aerospace P/N 6Y8207-00--1138 ea--Deliveries to Def Dep Ogden, Ut; DCSC Columbus, OH--RFP DLA600-82-R-0582--RFP due date 11 Feb 82--For technical info L. Lamb, 215/697-3457--See notes 73 and 55.

53--SEAL--NSN 5330-01-229-8823--Spec Coleman Seal Co. P/N AS09120--100 ea--Deliveries to NSC Norfolk, VA; NSC Oakland, CA; Def Dep Memphis, TN--RFP DLA600-82-R-0580--RFP due date 11 FEB 82--For technical info J. Creeden, 215/697-2435--See notes 73 and 55. (012)
Defense Industrial Supply Center, 700 Robbins Ave., Philadelphia, PA 19111, Tel 215/697-3668

53--VARIOUS SIZE RIVNUTS: blind, flat head/CSK head, open/closed end per source control drawings: SC-D-839807, SC-D-881873, SC-D-881879, SC-D-881080. Interested contractors are urged to request copies of solicitation packages promptly. Source control drawings require previously unapproved sources to comply with testing/approval requirements of the design activity as specified on the drawings in order to be eligible for award consideration. Approx. closing date 08 March 82. RFP DAAG99-82-R-0008. (011)
Tobyhanna Army Depot, Tobyhanna, PA 18464, Attn: Loretta Hash, SDSTO-AP-C, 717/894-7810

53--SEAL--Kinds Manufacturing Company Part Number 8035-21-MP3--RFQ 8-11-82-00333--NSN 5330-01-105-6833--five each--projected opening date 5 Feb 82--RFQ's are available--when requesting RFQ include this request for quotation (RFQ) number and enter the statement "request for RFQ" on the outside of the envelope. (012)
FAA, Mike Monroney Aeronautical Center, Purchasing Branch, AAC-73, P.O. Box 25082, 6500 South MacArthur Blvd., Oklahoma City, OK 73125 Attn: AAC-73A - Hall

● 53--PIN STRAIGHT HEADLE 7297043--NSN: 5315-00-887-6396--End use: M14 rifle--Quantity: 178,151 each--F.O.B. Destination--DAAA09-82-B-0395--Issue date o/a 18 Jan 82 with opening date 30 days from issue--See Notes No. 42 and 57--For bid info only Vernal Monson, 784-3186--Direct requests for solicitation packages only 309/794-P234 or 4186. (012)
US Army Armament Material Readiness Command, Attn: DRSAR-PCP-SP, Rock Island, IL 61299

53--PADLOCKS--USPS Item 5831--11,575 each--FOB destination, Pauline, KS and Somerville, NJ. LAW Federal Specification FF-P-101E, Amendment 1 & 2 IFB. No. 357100-82-A-2362. Bid opening date 2-8-82. (011)
Eastern Area Supply Center, United States Postal Service, VA Supply Depot, Somerville, NJ 08877

55 Lumber, Millwork, Plywood, and Veneer.

55--LUMBER, NSN 5510-00-235-0146, softwood, WW Fed Spec MM-L-751H Grade, various 124,789 bf. Destination, Camp Le Jeune, N.C. IFB DLA720-82-B-0194 Bid opening date 23 Feb 82. See notes 29, 30 and 50 (The size standard for this procurement is 500 people).

55--PLYWOOD, FSC 5530, ½ in., MW Fed Spec MM-P-530E dtd 10 May 77, Grade A-C, ext. 2000 sh. Destination, Camp Port of Loading (Hawaii) IFB DLA720-82-B-0188 Bid opening date 8 Feb 82. See notes 29, 30 and 50.

55--LUMBER, FSC 5510, softwood, MW Fed Spec MM-L-751H Grade, various 112,016 bf. Destination, Louisville, KY. IFB DLA720-82-B-0197 Bid opening date 4 Feb 82. See notes 29, 30 and 50 (The size standard for this procurement is 500 employees. (011)
Defense Construction Supply Center, Columbus, OH 43216, Attn: Bid Opening Officer, Tel 614/236-3449

55--WALL PANELING, Imitation Walnut Face, 4x8 Sheets--Issue date set for 18 Jan 82--Bid opening date 5 Feb 82-FOB McChord AFB, WA--IFB No. F45605-82-R00227 (011)
Base Contracting Office, P.O. Box 4179, McChord AFB WA 98438, Attn: Sfgt Rogelio, 206/984-2551

56 Construction and Building Materials.

● 56--CLAY-TYPE ASPHALT FOUNDATION COATING 56 drums for the Chouteau Ranger District, Chouteau, Mt. RFQ R3-4-5-83--Contract Time 45 Days--Bid opening 8 Feb 82, Room 308, Federal Building, Missoula, MT 59807. (012)
USDA, Forest Service, Lincoln National Forest, Federal Building, Alamogordo, NM 88310

56--ACOUSTICAL CEILING AND WALL MATERIALS 9 line items: Acoustical Tile Panels, 2x 4 x 48--4800 ea. Acoustical Tile Panels, 12 x 24--9000 ea--Main Tee, (aluminum) 12 ft sections--1470 ea--Cross Tee, (aluminum) 2 ft sections--6120 ea--Wall Angle (aluminum), 12 ft sections--110 ea--Perimeter Edge Angle (aluminum), 12 ft long--120 ea--Hanger Wire (12 gage, annealed/Galvanized) 10,000 LF--Acoustical Wall Tile Adhesive--20 Gal--Concrete masonry nails (3/16- dia x 1" long)--40 LBS. IFB F41621-83-B0009--Delivery to Kelly AFB, Texas--Issue date on/or about 02 Jan 25--Specifications will be furnished. (011)
AF Cryptologic Support Center/PWKI, Attn: Rose Terrell, San Antonio, TX 78243, 512/556-2021

56--INSULATION, THERMAL AND INSULATION BLANKETS, Various sizes, for delivery various GSA Depots within Continental U.S. Definite quantity contract. Std. No. 9FCC-89-56284. Scheduled to open: 2/2/82 (February 2, 1982) (011)
GSA, Region 6, Business Service Center, Building 41, Denver Federal Center, Denver, CO 80225

56--FLIGHT DECK COVERING, Mil Spec. MIL-D-21267 dated June 4, 1979 and CPL3136-38 dated Feb. 20, 1980. Stk No. 5810-00-141-7068. Various destinations. Definite quantity requirement. Std. No. 9FCB-TS-SAC11 scheduled to open: February 16, 1982. (012)
GSA Region 6, Business Service Center, Building 41, Denver Federal Center, Denver CO 80225

56--ALUMINUM HONEYCOMB, ALLOY 5052-CORE, per MIL-C-7438F, Grade B, Class 2, various sizes, perforated and non-perforated--IFB DAAD40-82-B-0000--opening o/o 23 Feb 82. (012)
Corpus Christi Army Depot, D/Adsts & Svcs, Procurement Div. Attn: Glenda Stenzebner (Ph 512/939-3572) Corpus Christi, TX 78419

58 Communication Equipment.

58--PROLIFERATED GROUNDWAVE COMMUNICATIONS SYSTEM (PGCS), Electronic Systems Division (ESD) is currently programming for acquisition of a CONUS-wide communications network to be implemented in the near future. The purpose of this network would be to provide US command and force elements with the ability to maintain critical C2 communications links in a stressed environment. This network would consist of up to approximately 600 unattended relay nodes, collocated, if possible, with existing commercial towers/antennas. Potential frequencies for this network would be either in the low frequency (LF) or medium frequency (MF) bands. The groundwave component of these frequencies would be designated as the carrier for relay message traffic between nodes. On 21 Jan 82 at 1000 hrs., ESD will present a classified briefing to potential offerors. This briefing will be held at the MITRE complex, Bedford, MA in Building 2, Room 1J103. The purpose of this briefing will be to allow potential offerors to become aware of the scope of system requirements, desired capabilities and program schedules as they presently exist. Firms responding to this announcement should mind the following requirements: a. have current technical experience in the areas of C2 integration and development of network systems; b. have current technical experience in the design and implementation of nuclear effects survivable electronic equipment; c. have current technical proficiency in either LF or MF networks. All potential offerors interested in attending this meeting must submit security clearances, along with intentions of attendance, in advance to ESD/XRC, Attn: Lt Jay Kenyon, Hanscom AFB, Bedford, MA 01731. Clearances must be received by ESD/XRC NLT close of business 19 Jan 82. No more than three individuals from each firm will be allowed to attend this meeting. Whether or not potential offerors plan to attend this meeting, letters of qualifications and capabilities must be received by ESD/XRC by 5 Feb 82. This synopsis is for informational purposes only, does not constitute an RFP and is not to be construed as a commitment by the Government. The Government does not intend to award a contract on the basis of this notice or otherwise pay for any information solicited. See note 68. (012)
Electronic Systems Division (AFSC) Directorate for Development Plans Deputy for Communications Planning (XRC) Hanscom AFB, MA 01731

● 58--PARAMETRIC AMPLIFIER, P/O CG-132A/WSC, NSN 5985-00-691-9001, WW Dwg. SM-A-717874-1 and cancellated. Qty to be relaged from 20 ea. to 120 ea. Delivery shall be 100 pst to New Cumberland, PA. IFB DAAB07-82-B-M479 will be issued o/a 1 Feb 82 closing o/a 1 Mar 82. See notes 66 and 43. Request DRSEL-PC-C-B-4, Kathleen Bernabei, (201) 532-3491.

● 58--TYPE 1297, teletypewriter, P/O TT-47B/UG, NSN 5815-00-110-4140, WW Pitman Electronics P/N LP1-5RA/AY, LP5RA/AY 157 and Teleconclusics Inc. P/N LP1-5RR/AY LP5RR/AY 157. Qty to be ralaged from 19 ea. to 114 ea. Delivery shall be 100 pst to Ludlow, CA. IFB DAA807-82-B-M339 will be issued o/a 15 Jan 82 closing o/a 15 Feb 82. See notes 44, 66, and 73. Request DRSEL-PC-C-B-4, Curtis S. Tobin, (201) 532-3491.

58--GEAR AND TUNER ASSY P/O AN/URR-71, 10 ea, NSN: 5820-01-008-4301 WW DWG DL-SM-8-7476SE. Del as follows: 7 ea to New Cumberland, PA 2 ea to Texarkana, TX; 0 ea to Lathrop, CA 2 ea to San Francisco, CA 1 ea to New York, NY. 43 ea RF tuner and amplifier assy P/O AN/URR-71 NSN: 5820-01-016-2134 WW Dwg DL-SM-8-747774. Del as follows: 4 ea to Lathrop, CA. 8 ea to New York, NY, 1 ea to San Francisco, CA, 30 ea to New Cumberland, PA. IFB DAA807-82-B-E101 will be issued o/a 15 Feb 82 with RFQ o/a 15 Mar 82. See note 66. Request DRSEL-PC-C-B-4, Anthony J. Manfredi 201-532-2362 (011)
U.S. Army Communications - Electronics Command, Fort Monmouth NJ 07703

58--PANEL spst to C 8011 control panel on F-15 AoS, NSN 5994 01 208 0774--42 ea lotty discount 56 ea, 75 ea). RFP F33600-82-00483 will be issued to GCI Systems Inc., Huntsville AL and Cincinnatian Precision Prod Inc., Willow Grove PA. Issue date will be on or about 21 Jan 82. See Notes 27 and 33.

58--SPARES spst to APG-63 System on F-15 AoS consisting of amplifier, NSN 5841 00 270 1489--25 ea lotty discount 22 ea, 41 ea); waveguide, NSN 5841 00 253 6821--21 ea lotty discount 34 ea, 39 ea) and window, NSN

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OFFEROR/SOLICITOR NOTICE
(ARRCOMC 715-5)

SOLICITATION NO. T1300

DATE 31 MAR 1982

ISSUING INSTALLATION/ORGANIZATION

DEPARTMENT OF THE ARMY
U.S. ARMY DEPARTMENT MATERIEL READINESS COMMAND
ROCK ISLAND, ILLINOIS 61299

NO. OF SOURCES SOLICITED

ITEM DESCRIPTION

NO. OF OFFERS RECEIVED

QTY	UNIT PRICE	SUCCESSFUL OFFEROR (S):
QTY	UNIT PRICE	

☐ NOTICE TO UNSUCCESSFUL OFFEROR

ALTHOUGH YOU WERE NOT THE SUCCESSFUL OFFEROR ON THE ABOVE INDICATED SOLICITATION (IFB/RFP), YOUR INTEREST IN GOVERNMENT PROCUREMENT IS APPRECIATED. IF ADDITIONAL INFORMATION IS DESIRED, IT MAY BE OBTAINED FROM THE ABOVE ISSUING INSTALLATION/ORGANIZATION OR BY HAVING A REPRESENTATIVE INSPECT AN ABSTRACT OF BIDS/OFFERS AT THE SMALL BUSINESS OFFICE OF THE CITED INSTALLATION.

☐ OFFER REJECTED

NO AWARD HAS BEEN MADE TO YOU SINCE YOUR BID WAS REJECTED FOR:

☐ SOLICITATION CANCELLED

- ☐ INADEQUATE OR AMBIGUOUS SPECIFICATIONS WERE CITED IN THE SOLICITATION.
- ☐ SPECIFICATIONS HAVE BEEN REVISED.
- ☐ THE SUPPLIES OR SERVICES BEING PROCURED ARE NO LONGER REQUIRED.
- ☐ THE SOLICITATION DID NOT PROVIDE FOR CONSIDERATION OF ALL FACTORS OF COSTS TO THE GOVERNMENT, SUCH AS COST OF TRANSPORTING GOVERNMENT FURNISHED PROPERTY TO OFFEROR'S PLANTS.
- ☐ OFFERS RECEIVED INDICATE THAT THE NEEDS OF THE GOVERNMENT CAN BE SATISFIED BY A LESS EXPENSIVE ARTICLE DIFFERING FROM THAT ON WHICH THE OFFERS WERE INVITED.
- ☐ ALL OTHER WISE ACCEPTABLE OFFERS RECEIVED ARE AT UNREASONABLE PRICES.
- ☐ OTHER REASONS:

☒ NOTICE TO REQUESTOR

WE REGRET THAT YOUR REQUEST FOR THE ABOVE SOLICITATION CANNOT BE HONORED; OUR SUPPLY OF SOLICITATION SETS IS EXHAUSTED. THE COMPLETE SOLICITATION IS PUBLICLY POSTED IN THE PURCHASING OFFICE OF THE ISSUING INSTALLATION. IN THE CASE OF A FORMALLY ADVERTISED PROCUREMENT AND A BIDDER USES HIS OWN BID FORM OR A LETTER TO SUBMIT A BID, THE BID MAY BE CONSIDERED ONLY IF (i) THE BIDDER ACCEPTS ALL THE TERMS AND CONDITIONS OF THE INVITATION, AND (ii) AWARD ON THE BID WOULD RESULT IN A BINDING CONTRACT THE TERMS AND CONDITIONS OF WHICH DO NOT VARY FROM THE TERMS AND CONDITIONS OF THE INVITATION.

TYPED NAME/TITLE/EXT	SIGNATURE
Mathew Ankney 4166	

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APR 7 1982

OFFEROR/SOLICITOR NOTICE

(ARRCOMC 715-S)

SOLICITATION NO. T1246

DATE 31 MAR 1982

ISSUING INSTALLATION/ORGANIZATION

HEADQUARTERS, U.S. ARMY ARMAMENT MATERIEL READINESS COMMAND
ROCK ISLAND, ILLINOIS 61299

NO. OF SOURCES SOLICITED

ITEM DESCRIPTION

NO. OF OFFERS RECEIVED

QTY	UNIT PRICE	SUCCESSFUL OFFEROR (S):
QTY	UNIT PRICE	

☐ NOTICE TO UNSUCCESSFUL OFFEROR

ALTHOUGH YOU WERE NOT THE SUCCESSFUL OFFEROR ON THE ABOVE INDICATED SOLICITATION (IFB/RFP), YOUR INTEREST IN GOVERNMENT PROCUREMENT IS APPRECIATED. IF ADDITIONAL INFORMATION IS DESIRED, IT MAY BE OBTAINED FROM THE ABOVE ISSUING INSTALLATION/ORGANIZATION OR BY HAVING A REPRESENTATIVE INSPECT AN ABSTRACT OF BIDS/OFFERS AT THE SMALL BUSINESS OFFICE OF THE CITED INSTALLATION.

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NO AWARD HAS BEEN MADE TO YOU SINCE YOUR BID WAS REJECTED FOR:

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- ☐ INADEQUATE OR AMBIGUOUS SPECIFICATIONS WERE CITED IN THE SOLICITATION.
- ☐ SPECIFICATIONS HAVE BEEN REVISED.
- ☐ THE SUPPLIES OR SERVICES BEING PROCURED ARE NO LONGER REQUIRED.
- ☐ THE SOLICITATION DID NOT PROVIDE FOR CONSIDERATION OF ALL FACTORS OF COSTS TO THE GOVERNMENT, SUCH AS COST OF TRANSPORTING GOVERNMENT FURNISHED PROPERTY TO OFFEROR'S PLANTS.
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TYPED NAME/TITLE/EXT	SIGNATURE
Mathew Ankney 4166	

ARRCOM FORM 65, 1 JAN 81

EDITION OF 17 MAY 78 MAY NOT BE USED.

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MAILGRAM SERVICE CENTER
MIDDLETOWN, VA. 22645

western union Mailgram

0-064687S018002 01/18/82 ICS IPMMTZZ CSP NYAB
1 2124416188 MGM TDMT RICHMOND HILLS NY 01-18 0859P EST

JAN 1[illegible]82

PITKIN MFG ATTN RONALD A PETERSON
3400 ATLANTIC AVE
BROOKLYN NY 11208

THIS MAILGRAM IS A CONFIRMATION COPY OF THE FOLLOWING MESSAGE:

2124416188 MGM TDMT RICHMOND HILLS NY 36 01-18 0859P EST
ZIP
COMMANDER PEARL HARBOR SHIPYARD
ATTN ELOISE FOWLER
BOX 400
PEARL HARBOR HI 96860
PLEASE FORWARD A COPY OF SOLICITATION NUMBER N00604-82-B-A110.
THANK YOU
RONALD A PETERSON PITKIN MFG 3400 ATLANTIC AVE BROOKLYN NY 11208

21:00 EST

MGMCOMP

Mr. PETERSON. My name is Ronald A. Peterson. I'm a small businessman employed as vice president and economist of Pitkin Manufacturing, Inc., a small manufacturing firm with 20 employees. We are located in the beautiful city of Brooklyn, N.Y., and the firm happens to be owned entirely by my family.

I am also president of the New York chapter of the National Tooling and Machining Association, an association engaged in contract work. A membership in the association is by company. Our membership totals nearly 4,000 member companies nationwide.

I very much appreciate the invitation of the committee to testify today. This is a matter that concerns my firm and our association in a very direct manner. The Commerce Business Daily is the sole source of information for small businesses enabling them to monitor Government contract opportunities.

The reason for this is simple. Small business is undercapitalized. With this financial constraint, it is simply impossible to afford sales representatives at any procuring activity let alone Washington, D.C.

Specifically, my own experience with the Commerce Business Daily began in the 1974–75 period. It was during the 1974–75 recession that my firm experienced a 50-percent drop in sales as a direct factor of the recession. We had been servicing an industry group which then turned toward Taiwan for all their machine part requirements in a cost-cutting measure.

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We decided at that point to try to locate a so-called recession-proof industry to service in the hopes of passing over any future recession and to keep a steady growth. We directed our efforts toward Government contract opportunities, feeling that that might be the recession-proof industry that we were looking for.

Being under the same financial constraints as all small businesses, the Commerce Business Daily became our sole source of information. In the past 7 years, I've been reading this publication on a daily basis. Now, speaking for myself, for the association, for all our members, I'm in full support of H.R. 5551. I see two major problems: One is the time constraints in the Commerce Business Daily, and the second is the synopsis appearing under the wrong classification within the publication.

It's rare that a synopsis today is published 10 days before the issuance of a solicitation. Furthermore, it is not uncommon at all first to see the synopsis only 20 days before the bid opening date. I have an example attached to my statement, and I'll just briefly refer to it.

In the January 14 issue of the Commerce Business Daily, there was an item for measuring tools, and the procuring activity was Pearl Harbor.

However, I received the Commerce Business Daily on the 18th by mail. It stated in the Commerce Business Daily that the bids would be opened on January 27. Requests for the solicitation set would be received no later than 10 days before bid opening. Well, 27 minus 10 is 17, and I received the Commerce Business Daily on the 18th. Nevertheless, I sent out—there is a copy attached to my solicitation—a mailgram requesting a bid set.

I sent out the mailgram that night requesting the bid set, and I received a copy of the bid February 1. Now, unless I had some unforeseen powers, which I obviously don't have as a mortal, I couldn't bid on that item. A factor which I think we must not overlook in the bidding cycle is a period that I refer to in my statement as the postal period.

Now, the postal period the way I've defined it here is the total length of time that bidding data are in the hands of the postal service. It really is four separate time periods. The first time is from the time the Commerce Business Daily is mailed to the subscriber—that's the first period, and it is not unusual at all to receive that 4 or 5 days after the published date. The second time in this postal period is when the subscriber or the bidder sends his request to the procuring activity requesting a copy of the solicitation set.

The third postal period is after the activity processes your request and puts that bid in the mail and sends it out to you. And the fourth period, of course, is after you've evaluated all your information and you are submitting your bid. You put it in the postal service for delivery to the procuring activity. Most procuring activities today request that you mail it 5 days before bid opening to insure receipt in a timely fashion.

I address particularly these four points from the manufacturers' point of view because each one of those four periods in which data are in the hands of the postal service, can easily take 5 days.

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Therefore, if a synopsis of the solicitation appeared 20 days before the bid opening date, and bidding data were within the hands of the postal service for three 5-day periods, because you've already received the Commerce Business Daily, you now have a grand total of 15 days elapsed. We then only have 5 days to respond to this bid.

In the case of the manufacturer, 5 days simply isn't enough time. I address the manufacturer's point of view because of the nature of my business and my association's business. The manufacturer faces many time-consuming tasks that a regular dealer or a distributor does not face. In the case of a regular dealer, he may call up his supplier and say, "What would my costs be for 2,000 micrometers?" He'd give them the cost and he could bid it accordingly.

A manufacturer would face many more tasks. I just want to present a quick example. An item that my firm had manufactured under contract for the Department of the Army is called the Bipod assembly. Basically all it is, is the Bipod that goes in the front of an M-16. It looks like a giant clothespin.

It looks like a relatively simple item—not many parts at all involved in it. However, if you were to submit a bid on the Bipod assembly and, of course, you are hoping to be the low bidder and receive an award of contract, you would have to obtain, let's say, three quotes from your suppliers, hoping to get the best quote on each different item.

Now, I would just like to give you an example of the items in this small assembly called the Bipod assembly, and I list them here as seven items. There is the steel which you need to fabricate the item. There are pivot pins which the two legs hinge upon; there is a steel washer in it; there is a spring in it. Heat treating needs to be done to the assembly. Phosphate coating needs to be done to the assembly, one by the metal treater and one by a finisher.

Also packaging, plastic bags and boxes. In addition to all this information which you need in order to properly bid for this item, you would also then, as a manufacturer, have to estimate your tooling time and costs and your production time and costs.

Now, keep in mind, due to the factor that I referred to as the postal period, you may only have 5 days in order to accumulate, correlate, and evaluate all this information in order to submit an intelligent bid. It is just simply not enough time.

You may ask, "If it's not enough time, how is bidding being done today?" Well, I am going to refer to something that may come as a shock to the committee, but there is a practice which is not uncommon at all today in business which is called low-balling. Low-balling is a practice by which a potential bidder or contractor would get a copy of the solicitation set, and then request from the procuring activity past pricing information. He may say, "Well, let's go back to the Bipod." He may say, "Oh, yes, the Bipod was procured last time last year. There were 1,000 units. It was $1 apiece."

You may get three or four of your key men in your firm together and take a look at it. "Can we manufacture that item? OK, we can manufacture it. What shall we bid?"

"Well, we don't have much time to get our quotes in. What was the last price? $1? Bid 99 cents. I think we can get it." That's low-balling. This is the attitude of that firm, "If we get the contract,

then we'll worry about all the little parts involved in manufacturing it."

Mr. MITCHELL. I promised not to do this, but this is intriguing to me, and I have to raise one question.

Mr. PETERSON. Sure, go right ahead.

Mr. MITCHELL. If you get the contract by low-balling, is there then another opportunity for you to revise the contract upward?

Mr. PETERSON. Pricewise?

Mr. MITCHELL. Yes.

Mr. PETERSON. Absolutely not.

Mr. MITCHELL. None? No shot at it?

Mr. PETERSON. No, no shot to revise that upward. The practice of low-balling is a dangerous practice for both the contractor and the Government. It will only lead the contractor down the path of financial destruction. There is no other way to get around it unless, by chance, he happens to hit a big one. The second thing is what it does in terms of the company. It hurts them because of the needed requirements the Government has that they are contracting for. This could cause serious delay. If the firm suddenly decided that they couldn't bid it or they couldn't manufacture it, there are ways a small business could go back to the procurement activity and claim problems with this and that, and have the contract rescinded. But this induces a tremendous delay into the system for the Government.

Another important factor of this is a crowding-out type effect. What it does is crowd out of the bidding process good qualified contractors. A good contractor obviously would not low-ball an item. He would go through all the steps meticulously. He would get all the information and bid it. After the third bid, if he sees No. 15 on the bid line, he's never down No. 1, he'll say, "Well, I've wasted an awful lot of time doing Government bidding, and this just isn't my field."

What you are doing then is crowding them out of the system because of the low-balling practice, which is really a direct effect of the time constraints presently in the Commerce Business Daily system.

I might add one other thing which wasn't in the testimony. There is another practice called high-balling. High-balling an item you would say, "How many people have bid on this item in the past?" If there are only one or two people that bid on it you say, "Well, here it is in the Commerce Business Daily. It's going to open in 7 days. Do you think anyone is really going to bid it?" "Well, what was the last price? The last price is $1. Bid $3. If no one bids it, we get it. For sure, if nothing else, we'll go back to the old contractor and get it for $1." This is shocking but it is a practice which is current.

To estimate the potential business which my firm has lost due to the time constraints and the problems with the Commerce Business Daily is hard because there are two problems. First, if a synopsis is classified wrong, there is a good chance you would never see that synopsis because we don't have that much time to go through each different classification within the Commerce Business Daily.

You may know well item 10, item 52, and item 56. Those are the ones I want to highlight every day, make sure I see every one. However, I would estimate that we've lost at least $500,000 worth of business in the past year due to just the time constraint.

Another point about why it's hard to estimate the amount of time is that you don't always receive a copy of the solicitation set from the procuring activity. I've attached to the back of my written statement just two quick examples of this. You might get back a notice to the offeror which says, "We regret that your request for the solicitation cannot be honored. Our supply of solicitation sets is exhausted." I've attached one from Rock Island. I also had one from the Tank Command in Warren, Mich.

Another problem is that you never get to see the actual drawings, the technical data to determine where you would have really fit in in that bidding process.

If they claim their solicitation set supply is exhausted, you are already crowded right out of that market.

I believe that the requirements of this legislation, H.R. 5551, will help eliminate these problems that I've outlined here today. The stipulation that proper notification be published at least 15 days before the issuance of a solicitation and then at least 30 days elapse before the bid is opened I believe will prove to be a very important benefit to small businessmen in the future.

In conclusion, I would like to add that I believe the legislation is in the best interests of both the Government and the small businessman. The Government will enjoy an increase in competition on its requirements with the side effect also of increasing the defense industrial base. The small businessman will also enjoy a greater opportunity of Government contracting. I think this is one of those situations in which everyone involved can come out a winner.

I would just like to briefly add three ways I see of improving the overall procurement system. One, by making the Commerce Business Daily available on a same-day type basis. I mean an on-line system, a data base, whereby a small businessman can take his terminal, dial up the number wherever it might be, plug in his computer and say, "Hey, let me see what is in the Commerce Business Daily." Through the electronic mails, in other words.

The second thing, if you found that there was only one specification that you didn't have in your file, and you would need to send away to the Naval Forms Publication Center in Philadelphia to get a copy of that, well, if you only had 5 days, just your request to the Naval Forms Publication Center would take more than 5 days and you would be knocked out of the ball game.

So I think a second way of improving the overall procuring system would be if we can have provided in the solicitation sets microfilm of the specifications needed to produce that job. And the third thing is just simplification of the solicitation in general. You may be procuring a steel washer, which is just a stamping, and it may be a 50-page bid. And you may then be procuring a breathing system, and it's the same 50-page bid. For the most part in my industry today, I'll have to say we are used to dealing with a verbal order where a firm may call you up and say, "Remember this part you once made for me?" "Yeah." "Well, make another thousand." That firm's word is as good as gold.

Or we work with just a one-page purchase order, that's all. You know, a reorder? And a lot of times our customers don't even put the new price down. They just write down in the places for price, "Please advise new prices." So today when small businessmen get in a 50-page solicitation, it scares them. You know, they say, there are a lot of things referred to in here, and I really don't have the foggiest of what they're talking about in there.

So, I do want to confine my statements here today in front of the committee to H.R. 5551. If you would like to discuss the possibilities of the other three items, please feel free to call upon me at any time.

I'd like to thank you, Mr. Chairman, and members of this committee, for my invitation to testify here today, and if you have any questions, I'd be happy to answer them.

Mr. MITCHELL. Thank you very much. I'm not a businessman. I must confess that I am now into the third month in reading the DAR requirements.

Mr. PETERSON. Yes.

Mr. MITCHELL. It's just so voluminous. I think if I were in business, I wouldn't ever try to do any business with defense.

The Administrator of the Office of Federal Procurement Policy recently testified before the Senate that he would attempt to enforce regulations which would require 10 days between the notice in the Commerce Business Daily and the issuance of the solicitation, and 20 days between the solicitation and the award of the contract. What is your reaction to his proposal?

Mr. PETERSON. Well, my reaction to his proposal is this: If he is going to try to enforce a regulation, that might be great. But to bend the regulation, I believe, is easier than to break the law, and I think that if this was law as opposed to being just a regulation, it would have an immediate impact on all procuring activities. I don't believe they would break the law. But as far as I understand it, right now, that regulation is in effect, and we are seeing it bent every day.

Mr. MITCHELL. He is saying 10 days versus the 15 days that's in our bill, and 20 days versus the 30 days that's in our bill. So you've already testified in support of our bill. That means that that approach is preferable to what the Administrator suggests.

Mr. PETERSON. Yes.

Mr. MITCHELL. We will be back in touch with you for your recommendations in terms of overall procurement problems. The gray that is in my hair is partly related to this God-awful business of coming up with a simplified method of procurement. We've now gone through the phase of reviewing the legislative proposal; I must confess that my first reaction to the latest OFPP proposal for these revisions in procurement is rather negative. It is still much too complicated.

So I think we have to come to people like you who have the expertise.

Mr. PETERSON. Well, feel free to call upon me.

Mr. MITCHELL. Thank you. Congressman Hiler?

Mr. HILER. Thank you. Several points I would like to ask Mr. Peterson. The low-balling is not going to stop just because there are more days. Right? I'm in business. Low-balling is always going to

exist. But it would seem to me that the advantage to having more days is to get more qualified bids. Not that you prevent low-balling—you are always going to have businessmen out there who don't have a handle on what they're doing. They're going to be faced with, "Geez, I need some business. I'm going to lay off people. Let's just bid."

It would seem to me that we would have to, in our competitive bidding, look at price, quality, and delivery. We have to look at all three and not just the price side. So hopefully, by expanding the time periods to respond, we bring more qualified bids in. But I'm not sure we'd eliminate the low-ball.

Mr. PETERSON. I'm not sure it would eliminate low-balling either. All I wanted to say is that it is easier to get more low-ballers in there than good qualified contractors if there is only a short period of time. In other words, a qualified contractor might say, "Well, there is just no way I could submit a bid if I only had 5 days. So why would I spin my wheels on this issue when I could look at another bid that might be coming up or another proposal for a contract."

Mr. HILER. How many bids do you get? You mentioned Rock Island. You've already done business with them. You are already on some of their mailing lists. Now, you get a certain amount of bid requests straight through, don't you?

Mr. PETERSON. I'm not sure I understood that. Do you mean that come straight from them.

Mr. HILER. Yes.

Mr. PETERSON. None at all. Absolutely not. The mailing lists today aren't worth the paper they're printed on.

Mr. HILER. I know they're not worth the paper they're printed on but you know, in the foundry business, we used to get stuff through direct all the time.

Mr. PETERSON. Is that right?

Mr. HILER. It was worthless, too.

Mr. PETERSON. Yes, well, maybe the foundry business, you might because, you know, especially today, you don't have too many foundries today.

Mr. HILER. We've got a lot of them. Not as many as we used to have.

Mr. PETERSON. We have a lot of machine shops around. If there is a machine shop out there, the way the system is, they revolve that bidders' list, and I guess maybe once every 10 years, you might get a bid.

Mr. HILER. So that's an ineffective way of getting the notice?

Mr. PETERSON. Absolutely ineffective.

Mr. HILER. You mentioned the data base. How many of your people in your association in New York would have the ability to plug into that data base or if that data base existed would plug into it and would make the purchase of the equipment?

Mr. PETERSON. Just speaking about the member shops in the New York area, I would say the average size shop in the New York area is maybe 20 employees. I would say currently half of them have computers in their office; and I would say at least one quarter of the other half are looking at computers right now.

I think if that were available, at least 90 percent would make a move toward it.

Mr. HILER. How much information would you have in that data base? Just the fact that this contract was up or would you try to put specs in there?

Mr. PETERSON. Oh, it would be absolutely beautiful if we could put specs in the data base. What I was referring to at first is just making the Commerce Business Daily available.

Mr. HILER. You could read it on it.

Mr. PETERSON. Yes, because a lot of times when you look at the Commerce Business Daily, you're only interested in certain classifications. In other words, you're not really interested in contracts for research and development, or for some type of water control system. You know what classifications you're into so you could just read it out.

Off the top of my head, I would say that's the first thing I would look for. After that, I think there is a wealth of information that could be used in terms of pricing information, contractors, past contractors on the job, specifications as you mentioned.

Mr. HILER. The Government is woefully behind in developing a computer data base. I'll ask a question that you can answer in any way that you see appropriate. Because of a variety of the kinds of stuff you have to go through to get a bid, how much extra does the Government pay for its tooling and its parts that it buys?

Mr. PETERSON. What do you mean by extra?

Mr. HILER. Well, let's say for the grief of putting up with the Government bid and overspeced—quite often, Government stuff is overspeced, particularly in the defense area—people add pricing. They add a price inefficiency that they have to deal with in defense procurement. Could you make an estimate of that? I mean, do you know any of your members who have had to construct new tooling when the new tooling wasn't needed?

Mr. HOHN. I could offer a little insight on that. There was an SBA study not too long ago, and they compared—I think it was 186 contracts—that had previously been sole source and were then competitively bid, and how effectively competitively bid in light of what Mr. Peterson has said is open to question.

But the saving was 50 percent. And in that same study, they estimated that if more contracts were open to competitive bid, the potential savings could be on the order of $1 billion in the defense area.

It is interesting to note that we are talking about the tip of the iceberg right now. We are talking about just the part that is competitively bid.

And just for example, I think it was in the same study, in spare parts alone—not major systems but just spare parts, only 7 percent of all the spare parts are competitively bid. Probably almost all of those could be competitively bid.

If anybody is interested in finding a way to save some money on defense, I would offer that for your consideration.

Mr. HILER. Well, I know it is quite often and the sole source of a markup is to take care of the fact that some of the Mickey Mouse they have to deal with in dealing with defense procurement, and the overspec. They overspec in cancelings, I know that.

Mr. PETERSON. I might be able to add a little more insight into your question, Congressman. Regarding the Bipod assembly which I referred to here before. In the last 10 years, we may have had four different contractors producing that item. The Government procured originally in 1969–71 the tooling.

And if you go from one stamping shop to another stamping shop, we probably have the same exact power presses. So you could take the tooling from that first shop and bring it to the next shop. I would say the tooling involved on a Bipod assembly would be $20,000. So if the Government had procured the tooling and then the tooling were passed on to other contractors, I would say it could have easily saved $20,000 on each shop along the way.

Instead, now, we have every shop tooling.

Mr. HILER. As you mentioned, Mr. Chairman, I'm not sure how you get a handle on it. It is just such a massive beast out there. You start slow, I guess.

Mr. MITCHELL. I think we have to pick away at it. Sole source at DOD has been the bane of my existence since I've been here. It really amounts almost to a monopolistic operation that is costly to everyone, not only in terms of those dollars but in terms of delays.

Well, that's another story.

Mr. HILER. Gentlemen, thank you very, very much. Mr. Director, thank you for your testimony and the other two gentlemen. I appreciate it. Thank you, Mr. Chairman.

Mr. MITCHELL. All right, while we are waiting for the next panel, I am amazed by the recent report of an 80-percent cost overrun in some naval procurement. The FBI is now investigating. It's an incredible figure.

Well, Mr. Creager and Mr. Holt. Mr. Creager is with the National Association of Small Government Contractors. Mr. Holt is representing the National Association of Aircraft and Communication Suppliers, Inc.

Gentlemen, again, my same apology for causing you to lose money by coming here. Every time a person takes a day away from his company, he loses some money. But we really want to avail ourselves of your expertise and your testimony.

Mr. Creager, would you lead off for us, please?

TESTIMONY OF WILLIAM A. CREAGER, PRESIDENT, CAPITAL SYSTEMS GROUP, INC.

Mr. CREAGER. Good morning, Mr. Chairman and members of the committee. My name is William Creager, and I am president of Capital Systems Group, Inc., a small business firm that I founded 13 years ago.

I am also a director of the Professional Services Council and of the National Association of Small Government Contractors. Both of these associations are vitally concerned with achieving effective and equitable Government procurement procedures.

Capital Systems Group is a Maryland-based professional services firm that provides information and management services to Government, industry, and the professions. Competitively awarded Government contracts constitute the main part of our business.

My experience as the head of a small business concern that deals extensively with the Federal Government has provided me with some viewpoints on H.R. 5551 and H.R. 6086, both of which are under consideration at this time by the committee.

On H.R. 5551, the announcements of procurement opportunities that appear in the Commerce Business Daily are a vital source of information to our firm. It is often said that if you don't know about a procurement until it is announced in the Daily, that it's too late to expect to win the contract.

This simply has not been our experience at all. Many of our current and past contracts have resulted from a procurement that we first learned about through the Commerce Business Daily. Now, in order for the Commerce Business Daily to serve our needs and to serve what I believe are the best interests of the Government, it must be complete in its coverage and it must provide sufficient time to permit the preparation of a proposal for a bid of winning caliber. I can only hope that all of the procurement opportunities that should be announced in the Daily are, in fact, announced. I have no evidence or suspicion that they are not.

However, the availability of sufficient time to prepare a responsive winning caliber bid or proposal is quite another matter. All too often we request bid documents announced in the Commerce Business Daily only to find that when we receive them, the due date is so close that our only choices are to submit a poor proposal or no proposal at all.

In such instances, we normally check with the contracting office involved to see if a time extension can be obtained, but the answer is usually negative. In most cases, it seems that the contracting office has established a closing date for the procurement, and then sends its information on to the Commerce Business Daily. Then, for some reason, the announcement in the Daily or the actual mailing out of the bid document is somehow delayed beyond the time the contracting officer had anticipated.

In other cases, it seems pretty clear to us, however, that a short time for response is deliberately established in order to limit the competitive response, possibly to one preferred firm. But whatever the cause, the absence of a reasonable period of time to prepare an adequate bid or proposal severely limits the Government's ability to select the best from among a number of well-prepared competitive alternatives.

It also acts to the disadvantage of those business firms, especially small business firms that depend on the Daily as the main source of information about impending Government procurements.

Those firms that do not depend heavily on the Commerce Business Daily as a source of information about procurements tend to be the larger firms with marketing personnel whose job it is to keep in direct contact with the various Government agencies and to monitor their procurement activities.

Small firms do not have such resources and do not have such forewarning. Our firm, for example, has no marketing or sales staff at all. Thus, I believe it is safe to say that smaller firms, as a class, are more dependent on the Commerce Business Daily as a source of marketing information than are the larger firms.

As it is currently drafted, H.R. 5551 would allow small businesses to compete more effectively against larger firms by giving them more time and opportunity, one, to order bid documents and with greater assurance of receiving them; two, to explore possibilities for joint bidding and subcontracting which are of vital concern to small businesses; three, to evaluate and better select among the procurement opportunities before them; and finally, to plan and prepare high quality bids and proposals.

For these reasons, I fully support this bill and feel certain that it will lead to more competition and better business proposals, and to more cost-effective procurement results for the Government and for the taxpayer.

On H.R. 6086, I would like to focus my comments on that one section of the bill that deals with the small business size standards. By requiring that changes in the small business size standards be handled in accordance with the Administrative Procedure Act, this bill would give the small business community the certainty of protection offered by law, that it now has only as a consequence of action taken voluntarily by the Small Business Administration.

Prudent action taken now could prevent a scenario from evolving that could be disastrous to the small business community. The scenario that could, conceivably, evolve in the very near future as the SBA attempts to implement rather wide-reaching and controversial changes in the small business size standards.

Beyond making this one change in the small business size standards, I would hope that the committee would take this opportunity to consider and to rectify some of the more fundamental and problematic aspects of the small business size standards as they currently exist. Some of the improvements I would like to see addressed are as follows: one, index those size standards based on the annual revenues to the inflation rate. These size standards have not been adjusted for several years despite double digit inflation in the interim.

As a consequence, many firms like ours have been squeezed out of their small business size status, not by real growth but just by inflation.

Two, require the Small Business Administration to develop and maintain materials and programs to train contracting personnel in the proper application of the small business size standards and to require agency contracting personnel to become proficient in this area.

All too often, we encounter contracting personnel who clearly do not understand what the small business size standards are and how they should be applied. We also encounter case after case where the different agencies apply different size standards to identical work.

Three, simplify the number and the structure of the size standards. Although we are a small firm confined to just 1 generic business area, we find ourselves competing for work under 10 different SIC codes and 5 different size standards. Ironically, at the same time, most of our work is categorized under what amounts to miscellaneous or services not elsewhere classified.

Finally, the size standards should recognize and allow for a phaseout from the small business size status. Much has been said

about the need to graduate minority firms from the 8(a) program, and to do this perhaps on a phaseout rather than an abrupt basis.

The same problem and the same need exists among all small businesses. Much of the benefit of the small business set-aside program can be undone when a firm such as ours suddenly finds that it can no longer bid on the same or similar jobs that previously made up the major portion of its business. Perhaps two or three tiers of size standards are needed to allow small businesses to become increasingly less dependent on the protection afforded them by the small business set-aside program.

Mr. Chairman, I appreciate this opportunity to appear before you today. Accompanying me is Mr. Harold K. Fletcher, president of the National Association of Small Government Contractors.

Mr. Fletcher has some further thoughts on these two bills that he would like to express at this time after which we would both be happy to discuss these matters further.

Mr. FLETCHER. Mr. Chairman, it is good to see you again. Thank you for inviting us. These are hard times for many smalls, and I think these two bills, H.R. 5551 and H.R. 6086, are clearly steps in the right direction. Our association was created especially to help small Government suppliers, and we think that the proposed legislation is going to do just that.

Regarding H.R. 5551 and the Commerce Business Daily, the CBD is often of marginal value, and I think by providing more time, we are clearly going to get better decisions and better proposals to support that fully.

My principal profession is as a consultant to small high-technology companies, and time and again they come to me and say, "Can we use the CBD? How do we best use it?" The extension of time and the enforcement of that time will clearly be helpful.

Regarding H.R. 6086, I am particularly interested in the increased financing to the SBIC's and the MESBIC's. I was a founder and a president of an electronics company in the late fifties, and ran it up into the early seventies. We did an early SBIC financing which gave us the financial strength to grow and retain earnings and carry the company to the point where we would take it public in the late sixties. It is that bridge financing that I think is so critically important to the SBIC program.

Some other comments on H.R. 6086. I agree with the notion of having SBA fully utilize its resources, but I think we also need to keep in mind the fact that SBA by charter has been asked to deal with marginal firms, firms that can't otherwise do for themselves all of the things that need to be done.

This, then, would suggest the need for agency and Hill dialog on failure rates, on guarantee ceilings, and on the numbers of smalls helped. Some of the things that I suspect SBA has done that underlie your new proposed legislation are encumbered by the SBA's fear of going to excessively high failure rates or not having enough guarantee authority to do all the bonding that they would like.

So, finally, I think you also need to push SBA to upgrade the technical qualifications and the focus of activities of its field personnel. I would like to see SBA encouraged to do more brokering of providing assistance so that the public sector takes advantage of

existing private sector institutions in providing necessary help to smalls.

Just a couple of examples. When I was SBA's Associate Administrator for Procurement Assistance, all 10 of our regional offices had as the Assistant Regional Administrator people who were qualified in Government contracting. Since I left Government 8 years ago, we're down to one who has Government contracting experience but is responsible for procurement and technology assistance; that's wrong.

You've got to have, particularly in these technical areas, competent leadership in order to deliver the programs that Congress intends. Another example: Certificates of competency, which are controversial in themselves. SBA provides the procurement assistance in issuing the COC, but they are not standing there with the financial assistance and the management assistance that's required to help this concern be successful and deliver what it contracts for to the Federal Government.

So I would encourage you to broaden your future hearings and consideration of legislation and include some of these other suggestions. I also would like to offer any help that I can be to you in the future. Thank you.

Mr. MITCHELL. Thank you. We will have some questions. Mr. Holt?

TESTIMONY OF LAWRENCE HOLT, EXECUTIVE VICE PRESIDENT, CONSOLIDATED AERONAUTICS CORP., LOS ANGELES; ACCOMPANIED BY JOSEPH PATRILLO, COUNSEL, NATIONAL ASSOCIATION OF AIRCRAFT AND COMMUNICATION SUPPLIERS, INC.

Mr. HOLT. My name is Lawrence Holt. I am vice president of Consolidated Aeronautics Corp., a Los Angeles-based corporation. Consolidated is also a member of the National Association of Aircraft and Communication Suppliers, Inc., and a manufacturer of military and aircraft spare parts.

I am also accompanied by Mr. Joseph Patrillo who is the counsel for the association.

I wish to thank this committee for inviting me to speak today on H.R. 5551 and the CBD or Commerce Business Daily, in general. I've been a regular reader of the CBD for over 20 years. I think its first issue was somewhere around the early 1960's.

It is important for you to realize how dependent small business is on a timely and adequate Commerce Business Daily. In our business, military aircraft parts, there are over a dozen separate defense procurement agencies scattered throughout the country.

It is not practical or economical for us or any other small business to have onsite representation in all of these buying offices. Therefore, we rely almost exclusively on a CBD to learn of contracting opportunities of $10,000 or more.

Small business is not the only beneficiary of the CBD. The Defense Department and other agencies are able to obtain competition because of publicity in the CBD. The competition translates directly into lower prices. Thus, the public reaps the ultimate benefit in the form of lower procurement prices.

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In our industries, the numbers are quite staggering. Over 90 percent of spare parts purchases for military aircraft are made without any competition. When competition is introduced, generally by small business, there are demonstrated cost savings of over 35 percent. Thus, many millions of dollars are at stake.

Effective publicity means more contracts for small business and more cost savings for the Government, but there is much more room for improvement in the CBD. The primary problem, of course, is timeliness. Current regulations give over 10 days between the date of publication and the issuance of a solicitation, but all too often, agencies don't observe these regulations.

Even when they do, however, the time limits are often not long enough. The majority of the procurements my company bids on are the negotiated type, and there are no regulations setting forth the minimum bidding period. In my experience, 10 to 14 days from the solicitation issuance is a common deadline for submitting these offers.

The total period for submitting offers is only 20 to 24 days from the date of publication in the CBD. However, very many more things must happen in that short period. First, we must receive the CBD by mail from Chicago. We must then review the CBD for items we may be interested in. Then we must request bidding documents from the procuring agency by mail.

Nothing can happen until we receive the documents from the agency, again, by mail. When we receive the documents, we must receive the item, review the data requirements and obtain the needed specifications and other information.

If we decide we can supply the part, we must compute a price, propose a delivery schedule and fill out all the necessary Government forms.

The final step is to transmit our offer to the Agency in sufficient time to arrive by the deadline. Thus, the 20- to 24-day period often shrinks to 2 or 3 days during which we must make all necessary technical and business decisions. We pride ourselves on a quick response time but frequently, 2 or 3 days just isn't enough.

When agencies don't comply with the time periods and the regulations, we are precluded from competing in any respect. Timeliness is the No. 1 problem that small businesses have with the CBD. We suggest the minimum period of H.R. 5551 be 15 days from the publication to request the bidding documents and 30 days to submit the offers.

Of course, procurements which are truly urgent would be exempt. A matter which deserves special consideration is the basic ordering agreement or BOA. Many purchases of aircraft parts are made from large businesses by orders issued under these annual arrangements. All of these orders are sole source, and made without any competition whatsoever.

Here the Commerce Business Daily is especially inadequate. Although regulations require that orders under BOA's be published in the CBD, many agencies routinely fail to do so; even when proposed orders are published, the regulations are applied to give only 10 days between the publication and the issuance of the order.

Thus, only 10 days after the Commerce Business Daily is sent from Chicago, all competition is precluded. Thus, the BOA, which

was adopted for administrative convenience, has become a device which can be abused to eliminate competition. Publication in the CBD can bring this practice to an end.

Therefore, I suggest the 30-day time limit, which is in H.R. 5551, would apply also to BOA's. Problems with the CBD do not end with timeliness, however. Some procurements sent to the Commerce Business Daily offices are never published. Apparently, this is because of lack of space but I find this practice inexcusable.

We pay about $130 a year for our subscription to the CBD. We would gladly pay more—two or three times more to make sure that we have an adequate publication. In addition, the synopses in the Commerce Business Daily are sometimes incomplete. They may not describe fully what is being purchased or whom to contact in the Agency for information and the bidding documents.

Such defects can be overcome by making inquiries, but this takes valuable time. If H.R. 5551 becomes law, proper implementation can insure that the procurement process is not any longer than it is now. Advance planning by the agencies should permit publication in the CBD early enough to avoid delay in the procurement cycle.

Surely, agencies should know what they are going to buy at least 45 days before they are in a position to award a contract. I thank you for this opportunity to testify and I'd be glad, again, to answer any questions after Mr. Patrillo makes his remarks.

Mr. MITCHELL. Thank you. My first question is to Mr. Creager. You indicated or recommended that there ought be some indexing between revenue size standards and the rate of inflation.

Generally, that idea is attractive, but I see some enormous problems in terms of the timespan under which you would look at the rate of inflation.

We've seen in past years the inflation rate go steadily up and in recent months, we've seen it go down. Are you talking about indexing on an annual basis or 2-year basis?

Mr. CREAGER. I would say probably annually. The situation as it has affected us is that most of our work is under a $2 million annual revenue size standard.

And a $2 million firm today simply is not the same firm that it was 3 or 4 years ago. Now, our growth has more or less kept pace with inflation but we've grown just enough to grow out of that $2 million size category. But we really are not, in effect, a large firm and we are not the same size firm we would have been had there been no inflation during that period.

So we have been kind of squeezed out of the small business size standard that is so important to our business just by inflation. I'm not certain that indexing is the best answer. It just seems to me, though, that in the past it's been up to the SBA, when they decide to do it, to do something about it, and I think it was maybe 3, or 4, or 5 years ago they changed what is now the $2 million size standard from $1 million. They just gave it a 100-percent raise. They haven't done anything now for several years, and the inflation rate has made a big difference.

Mr. MITCHELL. Well, I would just hope that if they attempt to make any further changes that it be done in full consultation with the small business community. I recall on this committee the last

time that SBA came before us with some arbitrary size standards; almost to a member, the committee said, "Now, look, this is simply not thought through well," and we rejected it. And I would just hope that if they propose any further changes that it be done in consultation.

You just can't make unilateral decisions within the agency without hurting a large number of our businesses.

Mr. CREAGER. In proposing changes in the size standards and some of the acts or actions we've heard about, SBA doesn't seem to have the reality of contact with the small business community in assessing what the impact some of these changes might be.

Mr. MITCHELL. Of course, it goes to the problem that you raise, and that's a matter of the technical upgrading, not only in the regional and district offices but right in central.

Mr. Holt, I'm just curious about one thing. You indicated that on many occasions, procurements are not even published in the Commerce Business Daily.

Mr. HOLT. That's true.

Mr. MITCHELL. How did you ascertain this?

Mr. HOLT. About 2 years ago, I made a trip to Tinker Air Force Base in Oklahoma. I was talking to one of the contracting officers and speaking about one of the Commerce Business Daily publications. And he said, "Gee, that's kind of interesting. I'm looking at it." He said, "That particular day, we sent in 20 things for procurements to be made to the CBD in Chicago." He said, "They only printed five."

I said, "Well, that's certainly not in the best interest of competition or small business, either, or the best interest of the DOD, or the public."

Mr. MITCHELL. When you learned that, did you attempt to contact Commerce Business Daily to try to find out why? You paid your bucks.

Mr. HOLT. Yes; we paid our bucks, but I think probably because of getting busy with different things, we started formulating our case on this H.R. 5551 at that time. I think this generally preempted the whole issue right from the start on that particular day.

But we see this continually, especially the Aviation Supply Office in Philadelphia which is the Navy Central Procurement Agency for all Naval aircraft spares. They will publish many, many BOA or basic ordering agreement requirements to the prime manufacturers, and those are never published in the Commerce Business Daily.

The reason that we know that as a fact is that we sell to Douglas Aircraft Co., for example, a lot of aircraft spares. Those procurements are over $10,000 each for separate procurements. They have never, ever been published in the CBD. It's been abused for many, many years, and I don't think it has ever been challenged, really, in all the years of its existence.

Mr. MITCHELL. The legislation that we have submitted does address the problem of the basic ordering agreement.

I thank you for mentioning that important aspect of the bill.

Mr. HOLT. The most important point the gentleman who was up here before us made is the statement that, as a rule, they can bend

the rules. But as a law, they are less likely to do so. They will obey the law.

Mr. PATRILLO. Could I also address this issue?

Mr. MITCHELL. Surely.

Mr. PATRILLO. I would like to allude to something the chairman mentioned earlier, and that is the offer by the Administrator of OFPP to enforce the regulations. I fear that there is less to that offer than meets the eye.

First of all, there is a 20-day bidding period alluded to in the offer. That bidding period in the current regulations applies only to invitations to bid which constitute fewer than one quarter of total procurements.

Second, the procuring agencies adamantly insist that the OFPP Administrator has no enforcement powers, and so he will not have willing objects of his enforcement or cooperative ones. Third, my own experience with the OFPP is they do a very, very good job there, given their staff. But they certainly don't have adequate resources to start enforcing procurement regulations.

Mr. MITCHELL. Thank you. It is an interesting point. In the back of my mind I was thinking of how ironic it is to talk about enforcing the regulations.

Apparently, no one does, and it is an ironic situation that we would have an Administrator of a Government agency, at least inferentially admitting that there is no enforcement of regulations.

Gentlemen, thank you. Thank you very, very much.

We have three more witnesses, and each one is in a specific category. So, we will hear from those witnesses one at a time, rather than in a panel arrangement.

Our first witness in this segment is Mr. Patrick Burns, from the Minority Equity Capital Co., Inc., speaking for the American Association of Minority Enterprise Small Business Investment Companies.

While both of you are here, I want to thank you for the tremendous help that you gave us in attempting to save the MESBIC's. At one point it looked like MESBIC's were about to go down the drain. There was a tremendous lobbying effort that took place, and for the moment at least MESBIC's are relatively secure. So, we publicly want to thank you for all of your prodigious efforts in that area.

TESTIMONY OF PATRICK OWEN BURNS, REPRESENTING THE AMERICAN ASSOCIATION OF MINORITY ENTERPRISE SMALL BUSINESS INVESTMENT COMPANIES; ACCOMPANIED BY JOANN PRICE, VICE PRESIDENT, AMERICAN ASSOCIATION OF MESBIC'S

Mr. BURNS. Thank you, Mr. Chairman, you have stolen half of my presentation because I wanted to thank, on behalf of the association, your committee in general and most particularly you for your efforts on behalf of our Association and through our Association on behalf of a group of several thousand minority entrepreneurs across the country who have come to rely for their business creation and expansion upon the resources made available through the MESBIC program. The association and our clients appreciate

very much your leadership and enthusiastic and intelligent support of the program and understanding of the complexities.

I suppose I should start formally. I am Patrick Burns, president of Minority Equity Capital Co. and chairperson of the legislative committee of the American Association of MESBIC's.

I have with me JoAnn Price, vice president of the American Association of MESBIC's. And I would like to publicly acknowledge an extremely effective vice president who provides very valuable leadership to our association in conjunction with many of your staff colleagues.

We have prepared and submitted a written statement which I will not go through, but I would like to submit it for inclusion in the record.

Mr. MITCHELL. Without objection it will be submitted in its entirety for the record.

[Mr. Burns' prepared statement and attachment follow:]

PREPARED STATEMENT OF PATRICK OWEN BURNS, BOARD MEMBER AND LEGISLATIVE CHAIRPERSON, AMERICAN ASSOCIATION OF MINORITY ENTERPRISE SMALL BUSINESS INVESTMENT COMPANIES

Good morning Mr. Chairman and members of the Committee. My name is Patrick Owen Burns and I am president of Minority Equity Capital Company, Inc. (MECCO) in New York. Accompanying me is JoAnn Price, vice president of the American Association of Minority Enterprise Small Business Investment Companies. Organized in 1971, MECCO presently has $2.6 million of private capital and has invested over $5 million in minority enterprises. In addition, MECCO's venture investments directly or in conjunction with other MESBICs triggered or served as the basis for over $50 million of additional capital, frequently for expansion. Our portfolio companies range from publishers, including Essence, to radio and television stations in a number of states including Tennessee, New York, Missouri, Pennsylvania, Georgia and Indiana, to manufacturing firms based in plants in Connecticut, Texas, New York and Vermont, serving a nationwide customer network to distribution and retail chains as well as construction firms.

As board member and legislative chairman of the American Association of MESBICs, I am here today to represent an industry of over 130 investment companies across the country.

MESBICs were created administratively in 1969 and through legislative mandate in 1971. Regulated by the Small Business Administration, MESBICs are specialized venture capital vehicles investing in minority-owned small businesses. Under the Small Business Investment Act of 1958, MESBICs are eligible for up to four tiers of leveraging from the SBA on their invested private capital. This private/public sector partnership serves to maximize

the pool of funds available for investment in the minority small business community at the same time it provides a personal incentive to seek out the highest utility of government dollars. Evidence of the broad-based support the MESBIC industry has received from the private sector is displayed in the attached chart, which lists several corporations that have invested in MESBICs, with the notable recent addition of International Paper Company.

In 1981 alone, MESBICs invested $25.8 million of private capital, combined with $28.5 million of SBA leverage dollars, for a total of $54.3 million targeted for the minority small-business sector. This amount provided for the financing of 742 businesses, whose total estimated revenue was $185.8 million. In addition, an estimated 3,749 jobs were created through 1981 MESBIC financing activity. The industry plans to increase the financial information available on MESBICs through our recent contract with Wharton Econometrics to establish a MESBIC data base.

Section 1 of H.R. 6086 increases the authorization level for the MESBIC program from $37 million to $41 million in fiscal years 1983 and 1984. With factors such as the high risk area of our investments, combined with today's high interest rates, this show of support for the industry is beneficial not only monetarily, but will insure the maintenance--and work to increase--the critical private sector participation and the continuity of a smooth private/public sector working relationship.

The accomplishments and continuing contributions to the American economy of the MESBIC industry have been recognized and acknowledged by the Administration through President Reagan's proposal for increased funding for the MESBIC program in his FY'83 budget. The nature of the MESBIC program is not only consistent with, but fundamental to, the goals of the present Administration--to maximize private sector participation in the economy. By the end of 1981, over $112 million in private capital had been invested in the MESBIC industry, nearly matching the government's contribution of $142 million. When capital attracted from other private sector sources by initial investments made by MESBICs are taken into account, the private/public funds ratio jumps to 6:1.

Congress, also, has indicated its continuing support of the MESBIC industry. Senator Nunn, of the Senate Small Business Committee, has recommended an even higher funding level than the Administration's for the MESBIC program in this year's budget. In the introduction of his legislation, Senator Nunn stated that the MESBIC program "fits perfectly into the Senate Small Business Committee's long-standing preference for programs which involve, and rely on, the private sector...The MESBIC industry is a stable, secure, and serious venture capital partner for minority businesses".

The MESBIC industry looks to you, Mr. Chairman, as one of our staunchest supporters in the House. The House Small Business Committee, under your leadership, has continually supported the MESBIC program, as evidenced by the subject of today's hearings.

Section 2 would require SBA to approve assistance in the maximum amounts permitted in appropriations Acts unless there is a lack of qualified applicants for assistance. The Small Business Administration requires MESBICs to adhere to certain requirements before eligible for leverage funds. They include: filing a complete application; demonstrating a need for funds (65% of funds must be committed or invested), an examination once a year by the SBA Inspector General's office and meeting credit and regulatory criteria. Those investment companies that meet this criteria should be able to obtain leverage funds within thirty to sixty (30-60) days. Two problems have complicated the smooth processing of leverage applications:

1. the Inspector General, as is required by law, is not able to examine all investment companies within a twelve month period. Delays in completing examinations have precipitated potentially damaging financing delays for the investment company.

2. when examinations are completed it has taken some MESBICs as many as three to six (3-6) months to receive their examination letters.

These two problems have created a situation where an investment company who applied for funds in fiscal year 1982 may not actually receive leverage until fiscal year 1983. This issue is of great concern to the Association and through the language proposed in this section we hope the problem is recognized and rectified.

Section 6 would require SBA to keep a record of the names and addresses and amounts requested by loan applicants or those who inquire about the loan availability of funding. The SBA presently has a policy of keeping thorough records on the SBIC industry, and we are happy with their present operations.

Section 14 requires that SBA size standards changes be in accordance with the Administrative Procedures Act. For the past 23 years, the SBIC industry has maintained a set of size standards separate from those of other SBA programs. SBIC size standards reflect the minimum criteria for public stock offerings, in recognition of the special role of SBICs as suppliers of capital to businesses which are unable to raise funds through public stock offerings. This underlines the major distinction between small businesses seeking 7(a) loans and firms requiring venture capital. Therefore, we feel it is important to maintain the separate size standard for the SBIC industry.

Finally, AAMESBIC would like to propose an amendment to H.R. 6086 on a vital issue that has arisen recently.

Under the Small Business Investment Act of 1958, as amended, MESBICs can receive up to four tiers of SBA leveraging on their "private capital". In an effort to promote the MESBIC industry, however, the SBA, in its regulations, allows for the inclusion of "nonprivate funds" in its interpretation of private capital for leveraging purposes. (See 13 C.F.R. 107.101(d)(2)(i).

Based on this provision, public funds, accompanied by large amounts of private funds, were being invested in the MESBIC industry for several years. These private funds were largely dependent for their effectiveness on the leveragability of the public funds they complemented. By mid 1980, over $17 million in government funds, in concert with over $10 million in private capital, had been invested in the MESBIC industry as a result of the public funds leverage regulation.

Then, in July of 1980, public funds leveraging was suddenly halted by a decision of the Comptroller General. The decision claimed the leveraging of MESBICs' federal funds to be illegal, except in the case of specific statutory language to the contrary. This decision was challenged and confirmed by a later Comptroller General's decision in January of 1981. Thus, the potential utility of over $100 million, targeted to one of this Administration's highest priorities, the small business sector, has been jeopardized.

The SBA's stance on this issue has been inconsistent and difficult to interpret. By delaying a formal reaction, it has incurred great costs on MESBICs with public funds. In some cases public funds MESBICs have been exposed to legal action taken by the businesses they had made commitments to based on their legitimate expectations of public funds leveraging.

We would therefore recommend that legislation be considered such that the words "private capital", as used in 15 U.S.C. 683(c)(2)(iii) of the Small Business Investment Act of 1958, shall be defined and interpreted to include not only capital which has been

raised from private individuals, partnerships or corporations, but also, for purposes of leveraging, non-private or public funds such as, by means of illustration and not limitation, funds received from the Department of Housing and Urban Development, the Economic Development Administration, the Federal Railroad Administration of the Department of Transportation, the Community Services Administration and others. Such interpretation of private capital shall apply only to those funds invested in MESBICs prior to a decision of the Comptroller General of the United States dated July 29, 1980. Such funds will retain eligibility for up to four tiers of SBA leverage.

Further, we recommend that 13 C.F.R. 107.101(d)(2)(i) be hereby ratified and approved insofar as it relates to those non-private or public funds invested in MESBICs prior to the above-mentioned Comptroller General's decision, and that the Comptroller General of the United States, the General Accounting Office and the Small Business Administration shall recognize and adhere to this decision.

Mr. Chairman, I would like to take this opportunity to express our appreciation of the continued support we have received from both you and your committee. I consider it a privilege and a pleasure to testify before you and would be pleased to entertain any questions you may have.

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The following companies have made significant investments in one or more MESBIC

Aetna Insurance Co.
Ameroda Hess Corporation
American Heritage Life Insurance Co.
American Motors Corporation
American Petrofina, Inc.
Amstar Corporation
Armour-Dial, Inc.
Arthur Andersen & Co.
Ashland Oil, Inc.
Associated Finance (Gulf & Western)
Atlantic National Bank of Jacksonville (Florida)
Atlantic Richfield Company
Bank of America
Bank of Virginia
Barnett Bank of Jacksonville, N.A. (Florida)
Bell and Howell Company
Black Methodists for Church Renewal
Boston Urban Foundation
Burger King Corporation
Burroughs Corporation
Campbell Taggart, Inc.
The Catholic Church
Central National Bank of Chicago
Chase Manhattan Corporation
Chemical Bank (New York)
Christian Broadcasting Network
Chubb Corporation
Combined Insurance Co. of America
Commonwealth Edison Company (Chicago)
Continental Illinois National Bank & Trust Company of Chicago
Control Data Corporation
Convenient Industries of America, Inc.
Cooperative Assistance Fund
Cottman Transmission Corporation
Crocker National Bank
Electronic Data Systems Corporation
The Episcopal Church
Equitable Life Assurance Society of the United States
Fidelity National Bank of Baton Rouge
Field Enterprises, Inc.
Fireman's Fund Insurance Company
First National Bank of Boston
First National Bank of Commerce New Orleans)
First National Bank of Dallas
First National Bank of Highland Park (Illinois)
First Pennsylvania Bank, N.A.
Financial Associates
Fluor Corporation
Ford Foundation
Ford Motor Company
General Foods Corporation
General Motors Corporation
Girard Bank (Pennsylvania)
Guaranty Bank and Trust Company of Alexandria, La.
Guaranty Bank and Trust Company of Lafayette, La.
Harding Associates
Hartford National Corporation
Hewlett-Packard Company
Humble Pipeline Company
Hyde Park Bank & Trust Company (Illinois)
IBM Corporation
I. C. Industries, Inc.
Illinois Tool Works, Inc.
Independent Life & Accident Insurance Company
Interlake Inc.
Irvinglake Inc.
Irving Trust Company (New York)
Interracial Council for Business Opportunity
International Telephone & Telegraph Corporation
Jacksonville National Bank (Florida)
Joe W. Brown Estate
Johnson & Johnson Company
John Hancock Mutual Life Insurance Company
John W. & Anna H. Hanes Foundation
Kaiser Aluminum and Chemical Corp.
Kresge's
Lomas & Nettleton Financial Corporation
MCA, Inc.
Maccabees Mutual Insurance Company
Marathon Oil Company
Manufacturers Hanover Trust Company (New York)
Marcor, Inc.
Marina City Bank (Illinois)

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Marine Midland Banks, Inc.
Metropolitan Life Insurance Company
Mobil Oil Corp.
Morgan Guaranty & Trust Co. of New York
National Can Corporation
New England Mutual Life Insurance Company
North American Rockwell Corporation
Northern Illinois Gas Company
Northern Trust Corp. (Illinois)
Olin Corporation
Opportunity Funding Corporation
Pan American Life Insurance Co.
Philadelphia National Bank
Phillips Petroleum Company
Prudential Insurance Company of America
Raskob Foundation
Republic National Bank of Dallas
The Riggs National Bank of Washington, D.C.
R. J. Reynolds Industries, Inc.
Mary Reynolds Babcock Foundation
Rockwell International Corporation
S. C. Johnson and Son, Inc.
Scott Paper Company
Sears, Roebuck & Company
Seattle First National Bank
Shell Oil Company
Society for Savings
Sohio Petroleum Company
Standard Oil Company (Indiana)
Standard Oil Co. of California
Stockton, Whatley, Davin & Co.
Sun Bank of Jacksonville
Sun Company Inc.
Swiss Colony Stores
Tech Mod Corporation
Trans Union Corporation
Travelers' Insurance Co.
Union National Bank of Arkansas
Union Oil of California
Union Planters National Bank of Memphis
University Computing Company
U.S. Trust Co. of New York
Valley Bank and Trust Company
Valley National Bank of Arizona
Varian Associates
Virginia National Bank
Wells Fargo Bank, N.A.
Winnfield Life Insurance Company
Worthen Bank & Trust Co. (Arkansas)
Wyly Corporation
Xerox Corporation
Zale Corporation
Zenith Radio Corporation

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Mr. BURNS. I will now simply highlight several points that we would like to underline. The first thing, just to give a little bit of flavor of what the MESBIC's are up to in preparing this testimony, we found out, a little bit to our surprise, that in 1981, the MESBIC program invested $54 million. Roughly half of that represented private sector resources, and the other half was the utilization of leverage funds from the Small Business Administration. Our surprise came, not that we were unaware of the activity of our 112 members, but that that number actually was an increase of $12 million from the previous year. In a terribly soft economy, I think this probably testifies to two things: One is that the energy and creativity of entrepreneurship continues, and that new businesses are, in fact, being formed and supported. That is all very positive. The MESBIC industry is standing in its traditional role of providing that capital to minority entrepreneurs.

On the negative side it probably represents an increased amount of trying to save the financially troubled businesses. I suspect that when we finally get the figures broken out, we will find that that category has a depressing increase. I know in our own case, our company has spent a more substantial amount of our investment funds in the last several years in support of troubled companies and trying to keep them reasonably stabilized than we have devoted to newly created companies and/or expanding, growing, prosperous companies.

We think in light of our own activities and the activities of the SBIC industry that the provisions in H.R. 6086 to set the leverage program appropriation for the MESBIC's at $41 million for the next several years and for the SBIC program at $250 million, are appropriate. Obviously, both of the programs would argue that, given our leadership role in business creation, and job creation, more could be utilized, but we understand the general constraints that the budgetary process has placed on all economic activity programs.

The increase this year proposed by this legislation for leverage, we think is a recognition of the role being played by the MESBIC community on behalf of its minority entrepreneurial clients. I think it is a very positive step in making available to the MESBIC community on a noncrisis basis the leverage which in fact, encourages the creation of additional MESBIC's, the expansion of those that exist, and serves as an important attraction for increased private capital coming into the program. We were not in this position last year when we, as you so properly indicated, thought that we were seeing the end of the program rather than intelligent and strong support.

So, we would underline our support of the leverage provisions. The second thing is that we would like to go on record as supporting the provision in the bill which would require SBA to spend the appropriated funds assuming qualified applicants.

As a little footnote to that, we would point out for the record two things: One, it has been our experience that SBA has not hesitated to spend appropriated funds, at least in the MESBIC program. But some of the regulatory procedures have cut against the spending of the funds. We have seen a number of our colleague companies get into a series of "catch-22" situations through the processing at SBA of leverage applications. One example: One of our colleagues had

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its application sent back 6 months after it had filed with a notation that its resolution from the board of directors was stale. Well, it was not stale when it was filed, but it certainly was 6 months later. So by the time it was refiled, you had a whole series of internal activities for which the company had to undergo financial reporting, plus the fact it got on the bottom of the pile again.

Mr. MITCHELL. Another 6 months.

Mr. BURNS. Another 6 months, that is right, so that to a certain extent it is disingenuous when SBA says that we have not been able to put the money out without telling you that they have applications in hand which if processed routinely and responded to promptly, would permit the full dispersal of the funds.

One of the problems that has developed recently is that SBA examinations have fallen further and further behind. We assume in part it is a manpower problem, but the regulations require a once-a-year examination in order to be eligible for leverage. Well, if your examination hasn't taken place in the 1-year cycle, you have to wait and wait. Then after the examination, if your comment letter is not received and responded to, you are, also, not eligible, and some of those letters have shown up anywhere from 2 to 4 months after the end of the examination which creates a sort of circular system.

One provision in the bill which would require the SBA to keep a record of inquiries and applications for funds we think is a sound idea. In our little corner of the world, in the MESBIC program, we have had satisfactory experience with SBA being able to track who has shown up looking for what. As I have indicated, our members have not always had satisfactory experience in the processing of the applications.

We do believe, as many of the previous witnesses have testified that the SBIC and MESBIC size standards should be handled the way that is being proposed in the legislation. We suffered with you and the members of the committee when this issue was last wrestled with, and we think perhaps we can, through the proposed legislation, perhaps put a punctuation mark on this problem and examine any size standard changes in an orderly and solidly procedural way. This would keep in mind the interests and needs of the small business community, as well as the realities of economic life.

Finally, although it is not part of the legislation, I am assured by Ms. Price that we, in fact, can suggest some things to be added. If she has misguided me, I will have to blame her after the hearing.

Mr. MITCHELL. Ms. Price never misguides anyone.

Mr. BURNS. That is what she tells me. We would like to suggest, and I know that you and your office are aware of this, as are members of the committee that, a problem has developed with a sizable segment of the MESBIC industry with regard to the leverage of publicly invested funds. These funds were committed to or were invested in companies in conjunction with private capital that was solicited and invested in expectation that the combined capital would be fully leveragable. It started out being leveragable, and it turns out, as you know, that there are four or five Government agencies at various times that have invested either directly or through an intermediary in the MESBIC program: HUD, EDA, the Railroad Administration of DOT and the Community Services Ad-

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ministration. Initially these funds were routinely leveraged, as I believe it was everybody's intention that they should be. But then as the activity became more comprehensive and extensive, varying views developed as to whether leverage should, in fact, be extended to Federal funds.

Well, this was an after-the-fact conclusion with the private sector funds already locked into place in anticipation that the totality of funds would be leveragable. This was an inducement to assume the risks of the kind of high-risk investing that our members undertake.

We would propose in this regard that the situation be clarified by grandfathering in those companies which presently have as part of their capital public funds, thereby making it clear through legislation that these funds, as I believe, everybody intended, would be eligible under SBA's normal rules and regulations for the appropriate amount of leverage. We do believe that we may be carrying too great a burden to argue that future Federal funds should be leveragable, other than inasmuch as Congress may in appropriating and designating such funds for MESBIC investment specifically say that they are leveragable. But as far as the funds presently in the program, we think that it is a needed resolution of a terribly confusing and unnecessarily confusing change and shift in policy, and would work to the substantial enhancement of minority companies looking for capital.

It is our estimation that the total leverage that we are talking about is on the order of $50 to $60 million which can go a good distance to meeting some of the capital needs of minority businesses.

Mr. Chairman, these are our general views on the legislation. I would again have the temerity to congratulate the committee on its expressed support of the MESBIC program which is increasingly important to the minority business community in a terribly troubled economic situation.

We welcome your support. We feel that our activities have given some indications of our deserving the support, and we hope that we will continue to deserve the support.

Mr. MITCHELL. Thank you very much. It has been one of my pleasures to have served in Congress long enough to have seen the MESBIC's evolve from a supercautious entity which did some good, but to a very limited number of firms, to the position which you now find yourself in, with $54 million invested. That is significant.

As one member of the committee, of course, I would support the grandfathering. I think that just makes good sense, but it appears to me that our real fight should be to change this ill-conceived new approach. It just makes sense to use public funds. I wish I could explain or understand some of the thinking that goes into these sweeping changes that are proposed overnight, but I cannot understand it. It seems to me that is where our fight is, to go back to the very sensible arrangement that existed in the past. So, pending that, I certainly would support the grandfathering in, and I think most members of the committee would. I would hope that most members of the committee would be committed to going back to the original proposition that was before us.

Mr. BURNS. Well, I think the entire underlying program, Mr. Chairman, is this public and private sector partnership, at various

levels of governmental activity. I think it has worked positively in the past, and I support your view that it should be affirmatively reexamined.

Mr. MITCHELL. Thank you. And Ms. Price, it is always good to see you.

Ms. PRICE. Nice seeing you, Mr. Chairman.

Mr. BURNS. Thank you, Mr. Chairman.

Mr. MITCHELL. All right, our next witness is Louise Dunlap from the National Association of Minority Contractors who is with the East Atlantic Construction Co. And my good friend Mr. Dewey Thomas is here. Good to see both of you again.

I thank you for having the patience and for waiting. We are up against severe time frames right now because I hope that we will act on a budget by May 15. Therefore, we have to get oral testimony and act on all bills prior to that date. So, thank you for waiting so patiently.

TESTIMONY OF DEWEY THOMAS, NATIONAL ASSOCIATION OF MINORITY CONTRACTORS, ACCOMPANIED BY LOUISE DUNLAP, SECRETARY-TREASURY, EAST ATLANTIC CONSTRUCTION CO.

Mr. THOMAS. Mr. Chairman, with your permission I would like to just make a few comments before Ms. Dunlap gets into her presentation. On behalf of our association and our board of directors, we want to thank you for the support that you have rendered contractors over the years and that our appearance here today is in support of both bills, H.R. 5551 and H.R. 6086.

One of the reasons why we chose Ms. Dunlap as a witness is because we believe hers is a company that exemplifies a need for the Small Business Administration. When SBA is not carrying out its duties, it does hurt her company very much. The company was created back in 1971 and has struggled through the years and is now seeing some very hard times because of the economy and, also, because of a lack of proper implementation of some of the SBA programs.

As you know, the construction industry is the largest industry in the Nation, and perhaps impacts more on the skilled and unskilled labor force more than any other industry. We want to make sure that the fruits of the labor put into this legislation also benefit minority contractors.

I would just like to bring to this committee's attention that we feel the MESBIC and SBIC sources of funds have been great over the years. They have been one of the only sources for new minority businesses in high-risk areas. But at the same time we feel that the construction contractors have been excluded from this source of financing. We feel that many of our companies now in financial trouble, would not be in this kind of trouble if they had had this source of financing. We would like to ask this committee to look into, or direct SBA to look into, creating some kind of pilot program for MESBIC's financing projects for construction companies.

There are many joint ventures that minorities have been involved in, but because of a lack of equity capital in that venture have not been able to play an equal role as relates to the profits.

So, we feel that if this were looked into that it would be very, very beneficial to minority construction contractors and, again, would lend to the credibility and success that MESBIC's have had over the years.

Mr. MITCHELL. May I interrupt you for just a moment? What has been the reason for the MESBIC's posture vis-a-vis minority contractors?

Mr. THOMAS. I think if Ms. Price was here?

Mr. MITCHELL. But, she has gone.

Mr. THOMAS. She could better address this than I. I am just speaking from my superficial knowledge of it. We polled the larger contractors within our association. None of them have any equity investments from MESBIC's or SBIC's. Regulations exclude MESBIC's from participating in project funding, and a construction company is built on projects. So, that is the clinker that prohibits this. Now, I know that there were either one or two pilot SBIC's for the movie industry. Movies are made one at a time, and I think if something similar was done for the construction industry that the benefits both to the private sector and the public sector would be great.

Ms. DUNLAP. Mr. Chairman, members of the committee, in addition to association views on H.R. 6086 I would, also, like to make a few comments as head of my company about problems with bonding. Business environment and confidence in the client are two of the most important factors in the bonding industry.

SBA's change of policy which reduced the maximum bond limit to $500,000 had a profound adverse effect on the ability of minority construction contractors to secure contracts. Mr. James Sanders, SBA's newly appointed Administrator is to be commended for his policy action of April 1, 1982, as follows:

(1) The maximum bond limit was restored to the legislative maximum of $1 million.

(2) The previous work experience requirement was amended to change the 125-percent limitation on new work to 200 percent of a previously bonded or successfully completed job.

We feel that a legislative prohibition against arbitrary limits on the surety bond guarantee program is needed and will be strongly supported by NAMC.

Since 1970, the surety bond guarantee program has been the lifeline for many small and growing minority construction contractors. The benefits derived by Government involvement can be clearly measured by the American taxpayer, the small business community and the private sector.

In addition to all the benefits derived from the surety bond guarantee program, we offer the following recommendation regarding problems needing your consideration.

The first problem is collateral. Two aspects of the SBA contracting program, surety bond guarantees and the guaranteed loan program should work hand-in-hand, but clearly they do not. The equal demand of the surety bond companies and the lending institutions for collateral security causes an impediment under present conditions. The subordination of all assets presents a "Catch-22" situation. Without a total asset security interest, both parties refuse to

move, thereby creating the situation of a no bond, no loan, no job; or, no loan, no bond, no job.

Through the programs mentioned the Government and the private sector can certainly devise some way to get the job done.

We offer the following suggestions for consideration and development:

One. Allow the surety company to have priority but not complete priority on all assets.

Two. Limit collateral available to banks for security to noncurrent assets, allowing such assets as accounts receivable and inventory to be unencumbered.

Three. Require all banks using the SBA guaranteed loan program to subordinate to surety companies.

Our company presently has a package with our bank for an SBA-guaranteed loan, and the bank is requesting security interest in all of the assets. The bonding company is requesting the same, and we have gone back and forth on it. The bank says that if the bonding company would subordinate to us, we will grant the loan; the bonding company says that if the bank would subordinate to us, we will give the bonding. We are at a standstill on it. The bank is supposed to meet tomorrow. We don't know how we are going to come out on it. I think the bonding company stated they would settle for access to the accounts receivable, but then the bank wants it all. So, if we had some legislation clearly stipulating who would have what, then we could avoid this kind of confrontation. Because in our situation we need the money in order to insure the bonding, and we need the bonding in order to do more work to pay back loans and to survive.

On the second problem, the bonding level was initially set at $500,000 in 1969. It was increased to $1 million in the early seventies. Since that time the present level has proven to be inadequate.

Our recommendation is that the committee review the adequacy of the present bonding level, taking into consideration the effects of inflation and other relevant economic factors, with a view toward increasing it.

Another problem is on the bonding data base statistics. There are no readily available sources of information concerning the performance of SBA surety bond guarantee programs.

Our recommendation is that this committee direct SBA to report quarterly on the performance of the surety bond guarantee program. Substantial statistical data could become a base for banks, surety companies, industry publications, such as Engineering News Records, and legislators to improve the decisionmaking process relating to minorities and the bonding industry.

Finally, we would like to state that some of SBA's actions and inactions, as well as the lack of timely communication with businesses and business advocacy groups have caused good SBA programs to be adversely criticized. Therefore, we continue to support this committee's vigorous oversight of SBA activities.

Thank you for your invitation to testify, and we would be happy to entertain any questions.

Thank you.

[The prepared statement of Mr. Thomas follows:]

PREPARED STATEMENT OF DEWEY THOMAS, NATIONAL ASSOCIATION OF MINORITY CONTRACTORS (NAMC), WASHINGTON, D.C.

Mr. Chairman, I thank you on behalf of the Board and members of NAMC for the opportunity to appear before your committee. I am accompanied today by Louise F. Dunlap, corporate secretary/treasurer of East Atlantic Construction Company, Washington, D.C.; a minority owned company, that started business in 1971. East Atlantic Construction Company's annual gross revenue is now approximately $2.0 million.

The National Association of Minority Contractors was started in 1969 to assist blacks, women, Puerto Ricans, Mexican Americans, Native Americans, and Asian Americans within the construction industry. The membership of NAMC has grown to 30 States, the District of Columbia and the Virgin Islands. The primary function of our association is to serve as an advocate for minority construction contractors.

The construction industry is the largest in the Nation. Our industry impacts greater on the American economy, particularly in the semi-skilled and skilled labor forces, than any other industry. Therefore, it is imperative that every minority contractor share and contribute in the fruits of this industry.

Mr. Chairman we would like to present our testimony in two parts: Part I—Address the program level of SBA; and Part II—Address the SBA surety bond guarantee program as directly viewed and experienced by Ms. Dunlap of East Atlantic Construction Company.

PROGRAM LEVELS: SECTION (1) OF H.R. 6086

The MESBIC and the SBIC government licensed capital companies have been outstanding sources of venture financing for new business, small business and high risk companies in growth potential industries. Most minority companies fall into these categories.

This financial resource is a prime example of the private and Government sector working together to improve the financial environment for small and new business, therefore we support the increased authorizations proposed for both MESBIC's and SBIC's in fiscal years stated.

PROBLEM

Because of existing SBIC and MESBIC regulations, construction contractors have been virtually excluded from this source of venture capital.

RECOMMENDATION

That this committee direct SBA to study the feasibility of licensing two pilot MESBIC's to exclusively develop and consummate venture capital financing opportunities for minority construction contractors.

BONDING

Business environment and confidence in the client are two of the most important factors in the bonding industry. SBA's change of policy which reduces the maximum bond limit to $500,000 had a profound adverse affect on the ability of minority construction contractors to secure contracts. Mr. James Sanders, SBA's newly appointed administrator is to be commended for his policy action of 4/1/82, as follows:

1. The maximum bond limit was restored to the legislative maximum of $1,000,000.

2. Previous work experience requirements were amended to change the 125 percent limitation on new work to 200 percent of a previously bonded or successfully completed job.

A legislative prohibition against arbitrary limits on the surety bond guarantee program is needed and will be strongly supported by NAMC.

Since 1970 the surety bond guarantee program has been the lifeline for many small and growing minority construction contractors. The benefits derived by Government involvement can be clearly measured by the American tax payer, the small business community and the private sector.

In addition to all the benefits derived from the surety bond guarantee program we offer the following proposed recommendations for your consideration.

PROBLEM: COLLATERAL

Two aspects of the SBA contracting program, surety bond guarantees and the guaranteed loan program, should work hand in hand; but clearly they do not. The equal demands to the surety bond companies and the lending institutions for collateral security causes an impediment under present conditions. The subordination of all assets present a "catch twenty-two" situation. Without a total asset security interest, both parties refuse to move, thereby creating the situation of no bond, no loan, no job, or, no loan, no bond, no job.

RECOMMENDATION

We feel that within the programs mentioned, the government and private sector can devise something to get the job done. We offer the following suggestions for consideration and development.

1. Allow the surety company to have priority but not complete priority on all assets.
2. Limit collateral available to banks for security, to noncurrent assets, allowing such assets as accounts receivable and inventory to be unencumbered.
3. Require all banks using the SBA guaranteed loan program subordinate to surety companies.

PROBLEM: BONDING LEVEL

The bonding level was initially set at $500,000 in 1969 and was increased to one million dollars in the early 1970's. Since that time the present level has proven to be inadequate in today's market places.

RECOMMENDATION

That the committee review the adequacy of the present bonding level, taking into consideration the effects of inflation and other relevant economic factors with a view toward increasing it.

PROBLEM: BONDING DATA BASE STATISTICS

There are no readily available sources of information concerning the performance of SBA's surety bond guarantee program.

RECOMMENDATION

That this committee direct SBA to report quarterly on the total performance of the surety bond guarantee program. Substantial statistical data could become a base for banks, surety companies, industry publications (ENR, etc.), and legislators to improve the decision making process relating to minorities and the bonding industry.

CLOSING REMARKS

In conclusion, we would like to state that some of SBA's actions and in-actions, as well as the lack of timely communication with business and business advocacy groups have caused good SBA programs to be adversely criticized. Therefore, we continue to support this committee's vigorous oversight efforts of SBA activities.

Mr. MITCHELL. Thank you. I really don't have any questions because we have worked together for so long, I think we are pretty much alike in our thinking. But on your recommendation with reference to the "catch-22" situation between the lending institutions and the surety companies, you made some good recommendations.

You are saying you would require all the banks using the SBA guaranteed loan program to subordinate to the surety companies. I can just see the banks lined up en masse, saying that no way in the world is that going to happen, are we going to allow the surety companies to have the priority on all assets. I could see most of the surety companies saying that look, we want it all, just as happened in your case. It is a tough question but it is one that has to be resolved. The kind of situation that you are confronting should be

able to be addressed under some provision of law. I just want to tell you that it is going to be a tough nut to crack.

Mr. Thomas?

Mr. THOMAS. We clearly understand that and just threw that out as food for thought. The big thing is that SBA, when they see fit, arbitrarily intercedes and does things administratively. In this case, we feel very strongly that they should intercede and act as a mediator between the two parties because they have a vested interest in the resolution. In other words, the bank is meeting tomorrow, but I venture there will be no one there from SBA to say that maybe we can do this in this case. We are really looking for SBA to intercede and play some role in this. SBA could resolve it and make everybody happy.

Mr. MITCHELL. Thank you. That clarifies it quite a bit.

Ms. DUNLAP. If the SBA is guaranteeing the loan at 90 percent, and is making a bond guarantee also, then the SBA has a vested interest and is taking the most risk on the small contractor. SBA could at least tell the banks and the bonding companies their position and help assure that we don't find ourselves in this situation.

Mr. MITCHELL. I must say that having met with the new Administrator, Mr. Sanders, on more than one occasion; I am impressed by the fact that he seems to be much more flexible than his predecessor. I certainly plan to meet with him on a regular basis. This will be one of the issues that I will put on the agenda for the next meeting. With the 90-percent guarantee, SBA has a big stake in this.

So, thank you for the recommendation. I thank you for your testimony.

Mr. THOMAS. Thank you, Mr. Chairman.

Ms. DUNLAP. Thank you.

Mr. MITCHELL. Gentlemen, I don't know to what church you belong, what faith you are; but in almost all the faiths it is said that the last shall indeed be first. It has been a long day for you, and I apologize, but we have no better way of handling it really.

Mr. Robert Schiffer, representing the Public Securities Association, Government guaranteed loan committee, and you are with Merrill Lynch, Inc.

I agonize over keeping people this long, but all I can do is apologize.

TESTIMONY OF ROBERT SCHIFFER, VICE PRESIDENT AND MANAGING DIRECTOR, MORTGAGE BACKED SECURITIES GROUP, MERRILL LYNCH, PIERCE, FENNER & SMITH, AND CHAIRMAN, GOVERNMENT GUARANTEED LOAN COMMITTEE, PUBLIC SECURITIES ASSOCIATION

Mr. SCHIFFER. That is quite all right. I will try to be very brief as a matter of fact, because I am sure you are all getting hungry.

Mr. Chairman, my name is Robert Schiffer. I am the vice president and managing director of the mortgage-backed securities group of Merrill Lynch. I assume at one point we were a small business.

Actually I am here today in my capacity as chairman of the Government guaranteed loan committee of the Public Securities Association.

The Public Securities Association represents most of the broker dealers and the dealer banks across the country who market U.S. Treasury and Federal agency securities, and securities issues by State and local governments. The committee which I chair represents substantially all of the firms in the Nation involved in providing a market for U.S. Government guaranteed loans for business.

I would today like to address my comments to the interest rate ceiling proposal contained in H.R. 6086. The Government guaranteed loan committee believes that the best and most desirable and efficient means of insuring the lowest possible cost of money for the 7(a) guaranteed loan borrower is not to impose any interest rate ceiling.

We believe that when an interest rate ceiling is imposed on a Government guaranteed loan program the natural tendency of the lender is to bump up against the ceiling. As a result, the small business borrower is not always able to receive the lowest possible interest rate on his loan. We also believe that without an imposed interest rate ceiling the strong competitive market forces would work to minimize the cost of borrowing for the small business owner as a lender would never be certain whether another competitor would underbid his offering. That is also my strong personal philosophy. However, things being what they are, we would like to compliment the committee on the interest rate provision in H.R. 6086. We know you share a belief that the small business borrower must receive the lowest possible interest rate on his 7(a) guaranteed loan, and in that regard we would like to make one suggestion to the committee regarding the 2¼ to 2¾ percentage point interest rate ceiling in the bill. As presently drafted, the bill would still permit the Small Business Administration to lower the maximum 7(a) guaranteed loan interest rate to prime rate. Such a possible action would have a devastating effect on the 7(a) guaranteed loan program, in that it would under certain market conditions, drastically reduce the volume of the SBA guaranteed loans,

That, in turn, would effectively preclude many prospective small business borrowers from obtaining long-term debt at any price.

Let me digress slightly from the text at this moment. That sounds slightly contradictory, but I do markets. I go to the ultimate borrower or the lender who supplies the money to the banks or whoever is going to lend to a small businessman. That is my job. In order to get the lowest interest rate possible, it is the first page of the first textbook, you must have a consistent flow of paper. You must have liquidity in the market. You must have people who are willing to stand there and say that I will buy the loan back; I will sell it to somebody else; I will transfer that paper from one area of more money to areas where money is needed. That is obviously the dealer function. That is what we do. Frankly, no matter how the paper is priced, I am still going to get my eighth of a point, my quarter of a point or whatever competitive forces allow in our business. But the fact is that the lower the rate to the small business borrower, the more paper there will be; the more paper there is,

the more interested the money manager, the pension fund, the source of funds is to lend the money at lower rates. It is an amazing thing. It works, but you know, I would rather see no ceiling at all because what it would do is, I think, bring in the competitive forces; but if there must be a ceiling, it must be a ceiling with an adequate spread so that the program is not turned off and turned on. I could go on forever, of course, about my personal opinion of using prime rate as a benchmark, but that I am sure you understand as well as I do.

Mr. MITCHELL. Our problem is defining prime rate.

Mr. SCHIFFER. Yes, you and I have the same problem.

We would like to suggest two additional means as an alternative. We suggest the interest rate ceiling be modified to give the lender absolute discretion as to what he charges. He, of course, has the ability to better underwrite the particular risk of a particular loan and therefore how much spread he needs to handle that type of business.

I think that could be handled administratively within SBA without particular legislation. We would like to suggest two additional means of reducing the cost of money to the borrower. First of all, the calculation of payments to the investor needs to be standardized as is already done in the mortgage-backed securities market which I have been involved with since the very beginning on a commission.

SBA has contracted with Bradford Trust Co. to be its fiscal and transfer agent, but Bradford lacks the authority to create a uniform schedule of payments to the investor. If Bradford were given that authority, it would increase the attractiveness of its certificate and the SBA guaranteed loan to the investor.

That increased attractiveness would lead to more investors competing to purchase Bradford certificates. Greater competition for the certificates as an investment would help insure lower interest rates to the borrower.

My point is if there is a dirty piece of paper, the investor feels that he has more paperwork behind it, therefore he is entitled to a higher yield. The cleaner you make the piece of paper that you are eventually going to hand the ultimate investor, fine; the happier he is, and the lower rate he will accept. Again, that is page 2 of the textbook.

Second, we believe the SBA should guarantee Bradford Trust's timely payment to the investor. This is much as Ginnie Mae does, as a matter of fact, with the mortgage bankers who create by the way, a very cost-effective program.

Again, this would help enlarge the field of potential investors in SBA 7(a) guaranteed loans. Taken together, these two proposals would go far to stabilize the secondary market. The benefits of a more stable secondary market could then, in our opinion, accrue to the borrower by as much as 50 to 100 basis points on his loan; and whether or not you need an explanation on basis points, it is a lot of money. It is a good deal of money in savings to the ultimate borrower.

Finally, Mr. Chairman, I would like to call your attention to a meeting tomorrow being held by a subcommittee of the SBA's National Advisory Council on the interest rate issue. Representatives

of the small business community, the secondary market, the banking community and the SBA will be convening to discuss ways of lowering cost of money for the small business borrower. Recommendations of this study group will be forwarded to the SBA National Advisory Council and then to the SBA Administrator.

Mr. Chairman, I appreciate the opportunity to testify before the committee.

I would be pleased to answer any questions.

[The prepared statement of Robert Schiffer follows:]

PREPARED STATEMENT OF ROBERT SCHIFFER, VICE PRESIDENT AND MANAGING DIRECTOR, MORTGAGE BACKED SECURITIES GROUP, MERRILL LYNCH, PIERCE, FENNER & SMITH, AND CHAIRMAN, GOVERNMENT GUARANTEED LOAN COMMITTEE, PUBLIC SECURITIES ASSOCIATION

Mr. Chairman, my name is Robert Schiffer. I am Vice President and Managing Director, Mortgage Backed Securities Group at Merrill Lynch. I am here today in my capacity as Chairman of the Government Guaranteed Loan Committee of the Public Securities Association. The Public Securities Association represents most of the broker/dealers and dealer banks across the country who market U.S. Treasury and Federal agency securities, and securities issued by state and local governments. The Committee which I chair, represents substantially all the firms in the Nation involved in providing a market for U.S. government guaranted loans to business.

I would today like to address my comments to the interest rate ceiling proposal contained in H.R. 6086. The Government Guaranteed Loan Committee believes that the best, most desirable and efficient means of insuring the lowest possible cost of money for the 7(a) guaranteed loan borrower, is not to impose any interest rate ceiling. We believe that with any government guaranteed loan program, when an interest rate ceiling is imposed, the natural tendency of the lender is to bump up against that ceiling. As a result, the small business borrower is not always able to receive the lowest possible interest rate on his loan. We also believe that without an imposed interest rate ceiling, strong competitive market forces would work to minimize the cost of borrowing for the small business owner as a lender would never be certain whether another competitor will underbid its offer.

Mr. Chairman, we would like to compliment the Committee on the interest rate provision in H.R. 6086. We know you share our belief that the small business borrower must receive the lowest possible interest rate on his 7(a) guaranteed loan. In that regard, we would like to make one suggestion to the Committee regarding the 2¼-2¾ percentage point interest rate ceiling in the bill.

As presently drafted, the bill would still permit the Small Business Administration to lower the maximum 7(a) guaranteed loan interest rate to the prime rate. Such a possible action would have a devastating effect on the 7(a) guaranteed loan program in that it would, under certain market conditions, drastically reduce the volume of SBA guaranteed loans. That, in turn, would effectively preclude many prospective small business borrowers from obtaining long-term debt, at any price.

As an alternative, we suggest the interest rate ceiling provision in the bill be modified to give the lender absolute discretion as to how much he will charge, up to the statutory maximum, as proposed in the bill. We believe that would be consistent with the Committee's intent to reduce interest rates and insure a viable 7(a) guaranteed loan program.

We would also like to suggest two additional means of reducing the cost of money to the borrower. First, the calculation of payments to the investor needs to be standardized as is already done in the mortgage-backed securities market. SBA has contracted with Bradford Trust Company to be its fiscal and transfer agent, but Bradford lacks the authority to create a uniform schedule of payments to the investor. If Bradford were given that authority, it would increase the attractiveness of its certificate (and the SBA guaranteed loan) to the investor. That increased attractiveness would lead to more investors competing to purchase Bradford certificates. Greater competition for the certificate as an investment should help insure lower interest rates to the borrower.

Second, we believe SBA should guarantee Bradford Trust's timely payment to the investor. Again, this would help enlarge the field of potential investors in SBA 7(a) guaranteed loans. Taken together, these two proposals would go far to stabilize the secondary market. The benefits of a more stable secondary market could then, in our opinion, accrue to the borrower by as much as 50 to 100 basis point on his loan.

Finally, Mr. Chairman, I would like to call your attention to a meeting tomorrow being held by a subcommittee of SBA's National Advisory Council on the interest rate issue. Representatives of the small business community, the secondary market, the banking community, and the SBA will be convening to discuss ways of lowering the cost of money for the small business borrowers. Recommendations of this study group will be forwarded to the SBA National Advisory Council and then to the SBA Administrator.

Mr. Chairman, I appreciate this opportunity to testify before the Committee and would be pleased to answer any questions.

Mr. MITCHELL. Thank you. I was not aware of the meeting tomorrow. I hope it yields some very positive results. As you know, our small businesses are just being clobbered right now.

Mr. SCHIFFER. Yes, they are.

Mr. MITCHELL. It really, in my opinion, amounts to an emergency situation. I hope we get some good recommendations and that they would be acted on with dispatch.

Mr. SCHIFFER. Yes.

Mr. MITCHELL. I cannot see this failure rate continuing for another year without it having a devastating impact on the entire economy. You indicate that SBA should guarantee Bradford Trust's timely payment to the investor.

Are you suggesting that there are some gross illustrations of nontimely payment?

Mr. SCHIFFER. It is not as consistent as one would want. Let me go back, if I may, to let us say, the mortgage industry.

Obviously, everybody's mortgage is due on the first of the month. When is the last time you paid your mortgage on the first of the month? You know, you get around to it on the fourth or fifth; we all do. It is a natural tendency. I think Ginnie Mae is a perfect example of how this has worked. The money is submitted at a certain date. It is calculated that it is there, and it is disbursed on the 15th of the month, and there is certainty as far as an investor is concerned. One of the gentlemen who was here before was talking about how we were woefully behind in our computerization. The world is woefully behind, and we all have our bureaucratic problems with our computers. There was a day when somebody said that a program would be finished on August 1, and we believed him. We no longer do that. But the fact is that the investor really wants to know that check is coming in on day such-and-such so they are set up for it.

They have money managers and pension plans and people like that who, by the way, are really the ultimate control of a great source of funds that are flowing back into the Government.

They are buying the Government-guaranteed securities. The flight to safety is here. We are seeing it right now. And so, therefore, Government guarantee or Government-insured programs are getting highest priority from these investors. But what they want is the cleanest piece of paper possible. So that the more standardization, the more liquidity; the more liquidity, the lower the rates. The lower rates, theoretically, will pass through to the ultimate borrower. It is just pure economics.

Mr. MITCHELL. I must say that when you first started your testimony I fell back against the back of my chair when you said to insure the lowest possible cost of money is not to impose any interest rate ceiling at all, but you have explained it.

Mr. SCHIFFER. Yes.

Mr. MITCHELL. However, I am so glad that you have given us an option because I don't think that would move anywhere in this Congress at this time.

Mr. SCHIFFER. Yes, I am aware of that, sir. I only wanted to make the point that I am a great believer in the process I outlined. I know the business, and I have no real ax to grind concerning the legislation. I do know how my side of the market works, and I know what I need to draw the money out to get it to where it has to be. So, therefore, as I say, there is a contradiction here. But the limits that you prescribed in the bill, fine, we support.

Mr. MITCHELL. Thank you very much.

Mr. SCHIFFER. Thank you very much.

Mr. MITCHELL. That is very provocative testimony.

Mr. SCHIFFER. Good. Thank you.

Mr. MITCHELL. I really appreciate it.

Mr. SCHIFFER. Thank you.

Mr. MITCHELL. I want to thank all those who have participated in this hearing. We have received statements for the record from any number of witnesses. I particularly want to note that Mr. Walter Stults of NASBIC waited patiently throughout almost all of the hearing and was kind enough to submit a written statement for the record rather than to testify.

[Mr. Stults' prepared statement follows:]

PREPARED STATEMENT OF WALTER B. STULTS, PRESIDENT, NATIONAL ASSOCIATION OF SMALL BUSINESS INVESTMENT COMPANIES

Thank you for inviting me to present testimony today on H.R. 6086, a bill authorizing program levels for the Small Business Administration for the fiscal years of 1983 and 1984.

I am Walter B. Stults, President of the National Association of Small Business Investment Companies (NASBIC), an organization which represents the overwhelming majority of all small business investment companies (SBICs) and minority enterprise SBICs (MESBICs).

As you know, both SBICs and MESBICs are privately-organized and privately-managed companies which provide equity capital, long-term loans, and management assistance to new and growing small business concerns. In return for agreeing to operate under the Small Business Investment Act and regulations issued by the Small Business Administration, SBICs are authorized to borrow from the Federal Government under a guarantee supplied by SBA. SBICs pay the full cost of money to the Treasury plus a premium for these borrowings.

As I said earlier, NASBIC represents both SBICs and MESBICs. Since you will also hear testimony from the American Association of MESBICs, I shall confine my remarks to the Section 301(c) licensees and the provisions in your legislation relating to regular SBICs.

WHAT HAVE SBIC'S DONE

The first SBICs were licensed in March 1959, just 23 short years ago, but I believe our industry has compiled a remarkable record of achievement in a little more than two decades. Let's look first at the overall numbers: SBICs have financed almost 50,000 independent businesses by providing over $4-billion in equity capital and long-term credit.

Despite all the problems which plagued independent business last year, SBICs disbursed more dollars in calendar 1981 than ever before—almost exactly one-third of a billion dollars. From a low of $123-million in 1975, SBICs have been more active each year and the total of $333-million in 1981 represented an increase of 170 percent in five years. I am pleased to tell you that our companies have maintained that active pace of investing this year. The records compiled by SBA's Investment Division show that we disbursed $108-million in the first three months of 1982, another all-time record and an increase of 40 percent from the first quarter of 1981.

A recitation of these straight numbers, however, tells only a small part of the SBIC story. To make a meaningful analysis of the worth of the SBIC program, we must look at it from two other perspectives: first, the value of SBIC dollars to small business; and, second, the cost of the undertaking to the Federal Government.

Two years ago, NASBIC commissioned the international economic consulting firm of Arthur D. Little, Inc. and the accounting firm of Deloitte, Haskins & Sells to study the economic impact of SBIC financing on the small businesses which received our dollars. As I have told this Committee in earlier testimony, that first study demonstrated beyond any question that SBIC assistance made a real difference: the average growth rate of SBIC portfolio companies was ten times greater than all American small businesses in terms of increased sales, employment, and profits.

So the first question about the worth of our endeavor is clear: small business makes good use of SBIC help. Let's turn to the second vantage point: how much does the SBIC program cost Uncle Sam? In this case, Deloitte, Haskins & Sells obtained financial data from SBA and used it along with the statistics it compiled for Arthur D. Little, Inc. in the earlier study. The accounting firm cranked out the numbers and found that the Federal Government received $110 in additional tax receipts for each $1 it spent to support the SBIC program. I must tell you that this cost-benefit number was so extraordinary that I told the officials of Deloitte, Haskins & Sells that I would have preferred a lower ratio, because I doubted whether anyone would believe the 110–1 benefit number. The firm went back and crunched the data one more time and concluded that its analysis was sound and placed its imprimatur on the study.

Only one month ago, Deloitte, Haskins & Sells performed one more permutation when it studied the cost to the Federal Government of creating a permanent new job through the SBIC program. This third study showed that the cost of job creation was only $312 for each new job. The accounting firm calculated that SBICs financed the creation of 147,730 new jobs in the ten years from 1970 through 1979. I submit that this is truly an outstanding record.

Mr. Chairman, I am submitting for the hearing record summaries of the three studies I have mentioned.

Before concluding this section of my testimony, let me share one or two additional statistical insights with you:

First: SBICs allocate a large share of their dollars to start-up financings. SBA data show that SBICs put 41 percent of their disbursements in firms one year old or less in calendar 1981.

Second: A large percentage of SBIC dollars are disbursed in the form of equity-type or straight equity financings. In calendar 1981, 35 percent of our dollars went out as straight equity, with another 32 percent in the form of debt with equity conversion features. For the first quarter of 1982, SBIC outlays were 41 percent in the form of straight equities (the highest ever) with another 32 percent of the dollars going for equity-type securities. Naturally, we are pleased that our industry is increasingly providing true venture capital to these new and growing businesses, in spite of the fact that our borrowings from the Federal Financing Bank are costing us much more than in earlier years.

To conclude, the SBIC program represents a unique, targeted economic initiative—it is the Federal Government's only effort in the venture capital field. The SBIC industry helps small business, creates jobs, stimulates private investment, develops new technologies, and generates added tax revenues. I guess I almost sound like an old-time medicine man peddling his snake oil, but I am in the fortunate position of being able to give you solid evidence backing each of these claims.

THE SBIC PROGRAM AND H.R. 6086

From my earlier comments on the accelerated pace of SBIC disbursements, it is apparent that our industry will seek an increased amount of borrowings ("leverage") from SBA during the coming months. Under present law, SBA will be able to guarantee only $160-million in leverage in fiscal 1983 and 1984. That is far too little to sustain our present rate of investment.

The squeeze is exacerbated by the fact that almost $155-million in outstanding SBA leverage will mature in fiscal 1983 and another $86-million in fiscal 1984. Under Federal budget accounting procedures, the "rollover" or refinancing of these maturing debentures count as if they were new loans, so the present ceiling on fiscal 1983 leverage could be virtually exhausted merely by a rollover of maturing leverage, leaving no borrowing ability for new licensees or for those SBICs which have not drawn down the dollars to which they are entitled by law.

Mr. Chairman, NASBIC believes that the industry could use as much as $250-million in new leverage in fiscal 1983 (in addition to the amount which will be required for refinancing maturing leverage), but we recognize the need to place limits on all Federal credit programs. For that reason, we support the $250-million total ceiling authorized by H.R. 6086 for both fiscal 1983 and 1984. We thank the Chairman and the members of the Committee for their continued backing of our program.

On the other hand, we shall continue to call attention to the proven effectiveness of the SBIC program in meeting so many of the Nation's fundamental economic policy goals. We know that our industry is cost-effective in creating new jobs for example, so we shall press both Congress and the Administration to utilize our capabilities fully whenever they seek efficient means for attacking unemployment.

One final observation and I shall conclude this portion of my testimony.

The availability of leverage is essential to the continued growth of the SBIC industry. If it appears that SBA will not be able to fill the needs of eligible SBICs for leverage, very few individuals or institutions will organize new SBICs and very few existing SBICs will increase their private capital. Obviously, such a scenario will impact most adversely on entrepreneurs seeking SBIC dollars to start new businesses and on owners of smaller firms requiring venture capital to expand their companies to bring new products and new services to the American economy.

COMMENTS ON OTHER SECTIONS OF H.R. 6086

Sections 2 and 6 of your bill, Mr. Chairman, provide that SBA would be required to utilize all of the amounts authorized by Congress except in those situations where the Agency did not receive sufficient applications from qualified borrowers. NASBIC supports these amendments to the Small Business Act and the Small Business Investment Act, even though I must say that SBA has never refused to extend leverage to SBICs when authorized to do so by Congress.

Section 14 of H.R. 6086 would force SBA to operate under the provisions of the Administrative Procedures Act when it wishes to amend its size standards. We believe this is an important safeguard for the small business community in general and for the SBIC and MESBIC industry in particular, so we support this section of your bill. One comment on this point: Section 15 of H.R. 6086 states that the Act would take effect on October 1, 1983. Would it not be better to establish a "date of enactment" effective date for Sections 2, 6, and 14?

CONCLUSION

This legislation is most important to American small business. I hope that my statement has adequately conveyed the positive impact of several of its provisions on the segment of independent business which requires venture capital for its birth, growth, and survival. Mr. McNeish and I would be pleased to try to answer any questions the Committee may have.

Thank you.

Mr. MITCHELL. It has been a good hearing. It is always a fascinating experience to me that when we come down to the fundamental hearings that affect the economy in a very significant way the attendance is rather sparse. But attendance doesn't make the hearing, it is the testimony, and it has been, in my opinion, excellent testimony uniformly from all of the witnesses. We will stay in recess until tomorrow morning at 9:30. Mr. Sanders of the SBA will be our witness for tomorrow.

[Whereupon, the subcommittee adjourned to reconvene at 9:30 a.m., April 29, 1982.]

H.R. 5551 and H.R. 6086

THURSDAY, APRIL 29, 1982

HOUSE OF REPRESENTATIVES, SUBCOMMITTEE ON SBA AND SBIC AUTHORITY, MINORITY ENTERPRISE AND GENERAL SMALL BUSINESS PROBLEMS, COMMITTEE ON SMALL BUSINESS,

Washington, D.C.

The subcommittee met, pursuant to notice, at 10 a.m., room 2359-A, Rayburn House Office Building, Washington, D.C., Hon. Parren J. Mitchell (chairman of the subcommittee) presiding.

OPENING STATEMENT OF CHAIRMAN MITCHELL

Mr. MITCHELL. Good morning. The hearing will now come to order. We had hearings yesterday on two pieces of legislation, H.R. 5551 and H.R. 6086. During the course of those hearings we had testimony on both bills. Three of the witnesses came from the city of Baltimore. When they left, the room then became filled with a visiting high school class from the city of Baltimore. In the hearing yesterday, I warned all of my opponents on Capitol Hill that we will keep our troops coming. I am well protected. So, this morning we have the students from Douglas Senior High School in Baltimore seated back there. They are here to observe a hearing. Also, they are protecting me. So, Mr. Administrator, and all of those associated with SBA, be on guard. Douglas High School students are here. They are on my side, and I would strongly urge caution on your part.

To the students from Douglas, thank you very much for visiting with us. I hope you will find the hearing enlightening and I hope you have a good day here.

Yesterday, we conducted a hearing on H.R. 5551 and H.R. 6086 and on modifications and additions to these bills contained in a committee print dated April 27, 1982. I will not again belabor the contents except to state that there is a summary explanation of the provisions available to interested parties.

At yesterday's hearing we received some excellent testimony from a host of private witnesses, who presented some one dozen legislative recommendations over and above the provisions contained in the pending legislation. I noted yesterday that the administration had one of their congressional liaison staff taking detailed notes on all the matters presented and I hope that these have been presented to today's witnesses so that they may be able to respond to the input they received yesterday.

This morning we are very pleased to receive testimony from the new Administrator of the Small Business Administration, Mr. Jim

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Sanders. Our congratulations and commiserations on your new appointment. I want to take this opportunity to congratulate him upon being selected and installed as the new Administrator and to welcome him before us this morning in what is his first appearance before the House Small Business Committee.

I want to note also that the small business community is facing probably one of the most difficult times in its history with record numbers of small businesses either filing bankruptcies or simply going out of business. The Administrator certainly has his work cut out for him, and I am looking forward to working with him to restore the viability of the Nation's small businesses.

I will ask the ranking minority member, Mr. McDade, if he has an opening statement.

OPENING STATEMENT OF HON. JOSEPH M. McDADE, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF PENNSYLVANIA

Mr. McDADE. Thank you, Mr. Chairman, I do and let me begin by echoing your welcome to your constituency from Baltimore. I want you all to know that Parren doesn't have any enemies in here. He has only friends, so we are delighted to have additional friends here this morning to be at the hearing.

And I want to welcome, in his initial appearance in front of the committee, our new Administrator. I, in my experience in Washington, have rarely seen an individual come to Washington to head a new agency to take charge in such rapid fashion. We are delighted with the improvement in the agency's performance. We are delighted with the new rapport that seems to have been established between the agency and Capitol Hill. We do have a series of challenging issues facing us, and I know that your career, both in the private and in the public sector, will stand the small business community well.

We look forward to a fruitful relationship with you, and we welcome you for your initial effort in front of the committee.

Mr. MITCHELL. Congressman Addabbo.

OPENING STATEMENT OF HON. JOSEPH P. ADDABBO, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW YORK

Mr. ADDABBO. Thank you very much, Mr. Chairman. I, too, want to welcome your constituents. I know in a few years they will be old enough to be voting for you. We expect you to be here for many years and I join my colleague from Pennsylvania in saying that you don't have any enemies, a few opponents, but no enemies.

Mr. MITCHELL. Quite a few.

Mr. ADDABBO. But I am happy they are here to see how, No. 1, the Government does work and, No. 2, how working within the system, you can make changes for the people you represent. And not only those people, but for the entire Nation and for the small business person and, in particular, the minority. So, I think a good lesson can be learned from watching your Government in action and, most important, watching our esteemed Chairman Mitchell as he moves this legislation ahead, which will help minority businesses and all small business. Some day you will be taking your right-

ful place in the mainstream, and this is what it is all about, to get all the people, all the Americans, within the mainstream.

For our new Administrator, I also offer my congratulations and condolences. I hope they painted the name on the door and didn't put it on with a sticker that they can just rip off because I think that is one of the most revolving offices we have, as far as administering is concerned.

I think one of the problems with that office is that it has been used as a political football in all administrations, not only this administration, but in past administrations.

I think for a change we have an Administrator who does come in with some background and some knowledge of the field and, most important, some feel for the people and for the agency that he will be serving and those who are affected by the agency. So, I wish you well and we offer you our cooperation. The other hat I wear, as you know, is defense and we will do everything we can to get help from defense to give you a little more to work with, both in money and the opening of various areas. As far as that is concerned, we have been successful in one battle. We have received a letter from the Secretary of the Navy today, announcing a change whereby they are trying to do umbrella contracting out, instead of contracting to individual small businesses, in many of our military installations; and we have put a stop to that, and hopefully will have it corrected.

So, I will look forward to continuing working with you here and, as I said, in my other committee. One thing I feel about this committee, and we have discussed this before, this committee has always been a nonpartisan committee because small business and the concerns of small business are not partisan things. Small business is 90 percent of the U.S. economy and affects all parties and all people. Therefore, on a nonpartisan, bipartisan basis, we try to support the administration, the Administrator of this agency and all small business.

So, in that light we will continue to be working with you. We will call you to task when you are wrong. We will praise you when you are right. I know the chairman and the other members of the committee and the subcommittees join me in saying many times you will be frustrated by the administration. You know what should be done, but you may need tools that this committee can give you, which you do not have. I would ask you to, if that be the case, communicate with this committee and we will help give you those tools, so that together we may help small businesses, especially minority businesses, become a part of the mainstream. I wish you well.

Mr. MITCHELL. Just before receiving your testimony, I think it is important to clear the air before we get to the question and response period. I have two very curious documents before me. One is dated March 29, 1982, from the Executive Office of the President, the Office of Management and Budget. It is signed by Mr. David Stockman, whom I think you know. In essence, it is saying in responding to specific questions on program and appropriation requests, witnesses will refrain from providing plans for the use of appropriations that exceed the President's request.

And it goes on to say that this change goes into effect immediately. That is from Mr. Stockman. The other curious document is from

the White House. It is a memorandum for the heads of executive departments and agencies and it is from the Budget Review Board, Mr. Edwin Meese III, Mr. James Baker and, again, our good friend, Mr. Stockman. Congressional inquiries about spending is the subject. It says in many instances representatives of your agency have been or will be asked by committees of the Congress how the agency might spend funds provided at levels in excess of the President's budget request. Because responses of such requests run the risk of having the President's budget misinterpreted, such responses should not be provided.

The last paragraph says neither this memorandum nor the revision of OMB's circular A-10 is intended to prohibit executive branch personnel from communicating with the Congress about the likely effects of decreases below the President's budget.

I am curious. In essence, it says that if any of the committees of the Congress ask you if you get more money how would you use it, you are ordered not to respond. If, however, there are questions about cutting further into programs, then you are perfectly free to respond to any decreases in social programs or funds for human needs.

Are you under such a rule, Mr. Administrator, before you begin your testimony?

Mr. SANDERS. Well, I think that the communication, Mr. Chairman, is quite clear. I do represent the President and the administration. We, in the administration, as you know, try to wrestle out our differences within the administration and then present to you a unified presentation, which, of course, you take and work over. I really feel that in our informal discussions, in our informal negotiations, that most of the important information that you need to compose your own ideas for the budget will be supplied or are supplied.

But it is quite clear that I do represent the administration this morning and I am free to discuss any kind of decreases below the proposed budget.

Mr. MITCHELL. Only decreases. With the understanding that the Administrator is bound when it comes to the question and answer period to respond to only questions that would further cut into our programs, we will now accept your testimony.

Mr. SANDERS. I might add, Mr. Chairman, that I would certainly hope that this doesn't provide a real obstacle to our communication, either here or unofficially, at any time.

Mr. MITCHELL. Oh, surely, I would not think that would happen. The sins of Stockman, et al., should not be visited on the heads of Departments and Administrators.

Mr. ADDABBO. Mr. Chairman, would the chairman yield?

Mr. MITCHELL. Yes; I would be delighted to yield.

Mr. ADDABBO. Mr. Sanders, along with that communique, if you were asked the question: What was your original submission to OMB, what was your original budget submission? Would you be able to answer that question or is that also prohibited?

Mr. SANDERS. Mr. Congressman, I think you are getting into an area that I would have to ask if I am within the administrative propriety to answer that without seeking some kind of legal advice. I have had this kind of problem. I think many of you are aware of

the underlying conflict. There are two opinions here that are in conflict about who has the constitutional authority to make these things happen. Does Congress have it and can they insist on this, or can the administrative heads of agencies, like myself, stand pat on the administration's proposals.

Let me assure you that I want to be cooperative in every way, that Congress is certainly entitled to all the information we have in the way we run our agency. I want to be totally cooperative in that manner. I guess I am going to have to say if you have any specific requests, I will certainly take them under advisement and, if I don't see any inhibition to furnishing those, I will get them back to you as quickly as I can.

Mr. ADDABBO. If the question was posed to you, you as an expert in the field of administration and small business matters, what would you feel would be the proper dollar amount to properly administer, or what would be the proper number of personnel to properly administer a certain responsibility, would you be able to answer those questions as Administrator or would that, again, be only your personal opinion?

Mr. SANDERS. I think once we define what the scope of the programs are, I can answer what I think the adequate level of resources would be.

Mr. ADDABBO. Your personal feelings or information or knowledge cannot be inhibited by OMB then?

Mr. SANDERS. I would be very pleased to share with you my personal observations on management approaches and our problems involved there.

[Communiques referred to above follow:]

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EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

March 29, 1982

CIRCULAR NO. A-10
Revised
Transmittal Memorandum No. 1

TO THE HEADS OF EXECUTIVE DEPARTMENTS AND ESTABLISHMENTS

SUBJECT: Responsibilities for disclosure with respect to the budget

This transmittal memorandum amends paragraph 4.d of OMB Circular No. A-10, Revised, dated November 12, 1976. Paragraph 4.d is changed to read:

> 4.d. In responding to specific questions on program and appropriation requests, witnesses will refrain from providing plans for the use of appropriations that exceed the President's request. Witnesses, typically, bear responsibility for the conduct of one or a few programs, whereas the President must weigh carefully all of the needs of the Federal Government, and compare them against each other and against the revenues available to meet such needs. Where appropriate, witnesses should call attention to this difference in scope of responsibility in explaining why it is not proper for them to support efforts to raise appropriations above the amounts requested by the President.

This change is effective immediately.

David A. Stockman
Director

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THE WHITE HOUSE

WASHINGTON

March 29, 1982

MEMORANDUM FOR HEADS OF EXECUTIVE DEPARTMENTS AND AGENCIES

FROM: THE BUDGET REVIEW BOARD
Edwin Meese III
James A. Baker III
David A. Stockman

SUBJECT: Congressional Inquiries About Spending Increases

In many instances, representatives of your agency have been or will be asked by Committees of the Congress how the agency might spend funds provided at levels in excess of the President's budget request. In the past, agencies have dealt with such requests in an ad hoc fashion. Because responses to such requests run the risk of having the President's budget misinterpreted, such responses should not be provided.

The purpose of this memorandum is to inform you that the Office of Management and Budget has revised OMB Circular A-10, which controls Executive Branch communications with the Congress about the budget, to ensure that all Executive Branch personnel who communicate with the Congress about the budget are informed of the Administration's policy in this area.

Neither this memorandum nor the revision to OMB Circular A-10 is intended to prohibit Executive Branch personnel from communicating with the Congress about the likely effect of decreases below the President's budget request.

OFFICE OF MANAGEMENT AND BUDGET
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Mr. ADDABBO. Mr. Chairman, I have to go to another committee, as you all know, and I have some questions I will be submitting for the record. Thank you.

Mr. MITCHELL. Thank you very much for being here. I know that Mr. McDade will have to leave shortly. Both of these gentlemen—indeed, all of us—are serving on many committees and it is getting to be a rather frenetic time in the Congress. So, Members will come and go, but I will be here.

[Questions referred to above follow:]

QUESTIONS SUBMITTED BY HON. JOSEPH P. ADDABBO TO SBA ADMINISTRATOR JAMES C. SANDERS AND RESPONSES

(1) How does the SBA Central Office determine the amount of direct loan allocations to each of its Regional Offices?

Is there a written formula for the allocation of such funds which this Committee could now review?

Are some of the direct funds allotted to the field earmarked for minority businesses? When did this practice stop? Why did it stop? How do you insure that minority firms receive their fair share of the direct loan money?

Answer. There is no written formula for allocation of direct funds. For some years, up to about three years ago, funds were allocated by state based upon population. This included a minority allocation. In the past several years allocations were based upon an approximate estimate of demand determined by historical usage of guaranteed funds. There were no minority set aside funds. However, goals were established for minority and women owned business loans. In March, 1981, all numerical goals were abolished in the loan programs upon a recognition that such goals were being perceived as quotas, resulting in the making of some loans where the borrower did not have a reasonable chance for success. It was recognized that approval of a loan in such circumstances constituted a disservice to both the borrower and the taxpayer.

At the present time, when loan demand is far below the supply of funds, there is no question that sufficient funds are available for all qualified borrowers including minority applicants. A plan has been proposed for the future to reserve a portion of SBA funds so that we may continue to be assured that funds will be available for all qualified minority applicants.

(2) Do you now impose direct lending goals on each of your field officers?

When evaluating the performance of your top managers in the field, is the amount of direct lending a performance criterion? Is it a criterion for any of your processing loan officers? Was it ever a criterion in the past?

Answer. At the present time there are no lending goals, direct or otherwise, imposed on field loan officers. The amount of direct lending is not a performance criterion for top managers. Although direct lending, as such, was not a performance criterion in the past, there were, up to last year, percentage goals established for minority and women owned business loans.

(3) According to statistics recently submitted by your staff to the Committee only about $53 million of the $89.5 million of direct loan funds allotted to the field during the last 6 months have resulted in loans. In fact, 17 of your district offices have made no direct EOL loans at all during the past 6 months. Why is this so?

Answer. We believe there are two principal reasons for this. First, loan demand is down generally, for all guaranty loans, direct loans, and for non-SBA loans at banks. Once again we believe this is due to the general state of the economy and high interest rates. Secondly, P.L. 97-35 raised SBA's interest rate on all direct loans (including LOL, but excluding HAL) to a formula rate presently 15⅝ percent. The purpose of this change was specifically to discourage artificial demand for direct loans, which made them virtually unavailable for those that really needed them because of the competition for loans at a subsidized rate.

(4) During our fiscal year 1983 budget hearing, SBA's excuse for not spending its direct loan money was that loan demand was down. I asked whether this conclusion was based on a reduction in loan applications, and how many applications were actually made to SBA. SBA's response, incredibly, was that their system does not tell them the number of applicants declined or those on waiting lists. If that is the case, how do you really know what your loan demand actually is?

Don't you believe a system should be in place to document loan demand?

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Answer. In reflecting on our discussion, I have determined that such information would be of additional assistance to the Agency in the management of our loan program. Therefore, SBA will be making available the following information on direct and guaranteed business loans:

1. Applications received during the month.
2. Applications screened out during the month.
3. Applications accepted during the month.
   a. Application approved.
   b. Applications declined.
   c. Applications withdrawn.

Data on loan applications pending at the end of the month are already available. Together, these data should provide SBA with an ongoing measure of the flow of demand for business loans, and establish an ability to be more responsive to information requests regarding this activity.

(5) If SBA continues to spend direct loan funds at the same rate it has over the previous 6 months (October 1981 to March 1982) what is your projected surplus at the end of the fiscal year? What is your projected surplus of guarantee loan authority?

Answer. If SBA were to continue to make loans at the same rate, the projected surplus at the end of the fiscal year would be:

(a) In direct loans approximately $96 million.

(b) In guaranty loans approximately $813 million.

(6) In a press release dated April 28, 1982 issued by your office, you are quoted as saying: "the entire agency is committed to the cause of bringing small disadvantaged businesses into the economic mainstream. For instance, we have recently announced that a goal of approximately 17 percent of our guaranteed business loans has been targeted for small minority firms, up from 9 percent in 1981."

In the first 6 months of this fiscal year a total of $24,000,000 in EOL guarantee authority was allotted to the field. Only $4,378,000 of this amount or 18 percent of the allocation was used. Since you have a $100 million program level requested, we can expect a surplus of over $91 million by the end of the year in the EOL guarantee program. Overall, we project a surplus of over $1 billion in all the guarantee lending programs.

In view of these facts, how does raising the goal on guarantee lending to minority businesses to 17 percent help minority businesses when banks aren't making guarantee loans in the first place? Isn't this just window dressing?

Answer. Although the surplus figures cited in this question are somewhat high, since April 1982 usage has increased, it is true that at the present rates substantial surpluses will exist. However, the 17% proposed plan is intended to reserve funds in periods of normal demand to assure the availability of funds for qualified minority applicants. It is not intended to be either a limitation on the funds available to minorities or an artificial attainment goal. The Agency remains committed to assisting disadvantaged businesses and, in this case, is attempting to insure that adequate funds will be available to accomplish this end.

Mr. MITCHELL. Mr. Administrator, we would be delighted to hear from you at this time.

TESTIMONY OF JAMES C. SANDERS, ADMINISTRATOR, SBA; ACCOMPANIED BY DONALD TEMPLEMAN, DEPUTY ADMINISTRATOR; EDWIN T. HOLLOWAY, ASSOCIATE ADMINISTRATOR FOR FINANCE AND INVESTMENT; AND HARRY CARVER, COMPTROLLER

Mr. SANDERS. Thank you, Mr. Chairman. With your kind permission, I will read the statement that I have prepared for the committee.

Mr. Chairman and honorable members of the subcommittee, it is an honor and a pleasure to appear before the subcommittee today. This is my first appearance before a House committee as the Administrator of the Small Business Administration. I have had an opportunity to meet with many of you prior to my confirmation and I look forward to getting to know you all better and working with you for the betterment of small business.

Appearing with me today is the Deputy Administrator, Donald Templeman; the Associate Administrator for Finance and Investment, Edwin T. Holloway, and the Comptroller, Harry Carver.

You have invited me to discuss with you three bills that are pending before this subcommittee. The first one is the Commerce Business Daily, H.R. 5551, introduced by you, Mr. Chairman, and Congressman Ireland. This bill would amend section 8(e) of the Small Business Act by providing that whenever a procuring agency is required by that section to publish a notice of procurement action, it must, one, allow 15 days from the publication of the notice to the issuance of a solicitation for procurement, and two, a minimum bidding time of 30 days.

Currently, whenever a Federal procuring agency is required to publish a notice of a procurement action in the Commerce Business Daily, a solicitation for bids on that procurement should not be issued until at least 10 days have elapsed from the date of publication. The proposed legislation would increase this to 15 days and, in effect, cause this provision to be mandatory, vis-a-vis, permissive. Also, current regulations provide for a minimum bidding time of 20 calendar days in most instances, whereas H.R. 5551 would provide at least 30 days from the issuance of a solicitation before a bid is opened, in all cases.

Federal procuring agencies, even now, where currently the minimum requirements for CBD synopsizing are "not later than date solicitation is issued," and where solicitation time, from issuance to closing, is more than 15 calendar days, are not fully complying.

SBA surveillance reviews have consistently revealed over the years substantial noncompliance by contracting officers with regulatory CBD synopsizing guidance. These findings are reported to Federal procuring agency heads. This continuing problem still remains with us today, and until recently, little, if anything, had been done to bring about compliance at the buying activity level.

Last month, Donald Sowle, the Administrator of the Office of Federal Procurement Policy, testified in the Senate on identical legislation, S. 1947. He told the committee that the problem can be resolved by adherence to current regulations. Administrator Sowle made a commitment at that hearing to improve and give special emphasis to regulations concerning publication of proposed procurement. He has offered to work with the SBA on this matter. Accordingly, the administration opposes the legislation at this time, pending a fair test of OFPP's determination to bring about proper implementation of the existing regulations.

H.R. 5953 is a bill submitted by the administration and was introduced by you, Mr. Chairman, by request. It would raise the authorization level for SBA guarantees of loans that further the policies established in section 2(c) of the Small Business Act, with particular emphasis on the preservation or establishment of small business concerns located in urban or rural areas with high proportions of unemployed or low-income individuals or owned by socially and economically disadvantaged individuals.

Such loan guarantees would be increased from $60 million in fiscal year 1982 to $100 million and $60 million in fiscal years 1983 and 1984 to $167 million in each of those fiscal years. It would also increase the authorization level for SBA to purchase debentures

and preferred securities from minority enterprise small business investment companies to $41 million in each of the fiscal years 1982, 1983, and 1984, from the present level of $35 million for each of those fiscal years. This bill reflects the present position of the administration and, therefore, the SBA supports its enactment.

Mr. Chairman, I should note that this Tuesday the committee informally made available to SBA a committee print containing new provisions on high unemployment area direct loans and on new labor surplus area procurement. The print also contained revisions of certain sections of H.R. 6086. Inasmuch as this did not allow sufficient time to analyze this new material, my comments today will be limited to the contents of H.R. 6086 as introduced. I will, of course, be pleased to provide written comments on the new material for the record, if the committee wishes.

Now, on H.R. 6086, introduced by you, Mr. Chairman, it is a multifaceted bill which would affect several of the SBA's programs by amending multiple sections of the Small Business Act and the Small Business Investment Act. Section I of the bill would alter several of the authorization levels for SBA's programs. It would raise the amount of loans authorized to be made to further the policies set forth in section 2(c) of the Small Business Act, with particular emphasis on the preservation or establishment of small business concerns located in urban or rural areas with high proportions of unemployed or low-income individuals or owned by low-income individuals. It would also authorize $250 million, rather than $160 million in fiscal years 1983 and 1984 in guarantees of debentures for the programs authorized by title III of the Small Business Investment Act.

SBA must oppose the SBIC authorization increase because the amended levels would exceed the administration's credit budget and threatens the President's efforts to mitigate the adverse effects of Federal intervention on credit markets. The rest of the increases are reflective of administration policy and the SBA endorses them.

Section 2 of H.R. 6086 would require that SBA operate all of its guaranty programs—including guarantees of loans, debentures, payment of rentals, surety bonds, and other types of financial assistance—in the full amounts provided by law, subject only to the availability of qualified applicants and limitations contained in appropriation acts.

On first impression, this provision would seem perfectly reasonable. But I believe that on further reflection it should be clear that enactment of this section would create a serious impediment to the sound management of the Federal Government.

Any organization needs to be able to adapt to changes in its environment. This is especially important for the Federal Government because of its role and size. The Government must have the flexibility to adjust program levels as a result of changes in economic conditions or in needed changes in program mix, intra- and interagency coordination and unforeseen events. So, therefore, the administration opposes this provision.

Section 3 of the bill would amend paragraph 1 of subsection 404(b) of the Small Business Investment Act by requiring that guarantees of contracts for pollution control facilities shall be issued when the property is acquired by the use of proceeds from

industrial revenue bonds which provide the holder's interest which is exempt from Federal income tax, and it prohibits SBA from withholding such a guarantee when the property is so acquired. The administration opposes enactment of this provision on the grounds that it allows a double subsidy, a matter which other administration spokesmen have addressed in testimony.

Section 4 of the bill would specifically prohibit SBA from establishing eligibility criteria for its surety bond guarantee program based on the amount of the bond to be guaranteed, or upon a percentage related to previously successfully completed contracts. It also requires SBA to evaluate each surety bond application on a case-by-case basis, and based thereon determine the appropriate percentage guarantee. This provision is also intended to overturn present SBA procedures relative to the surety bond guarantee program. As such, we oppose it. We maintain that the use of the amount of the bond and percentage related to successfully completed contracts are worthwhile eligibility criteria for the program within the context of current budgetary realities.

If this bill is enacted and signed into law, we would have no choice but to stop using these criteria. We cannot favor what amounts to a legislative management of programs, particularly when we feel programs are being administered in accordance with the existing legislative mandate.

Section 5 of the bill would replace the current statutory language for establishing the interest rate for SBA guaranteed loans with the New York prime rate plus up to 2¼ percent for loans of 7 years or less maturity, and up to 2¾ percent for loans of 7 or more years of maturity.

This amendment would statutorily require the SBA to use what it presently has chosen to use as the interest rate for guaranteed loans as established by regulation. However, we cannot favor its enactment because it would lock us into a rate which might become unrealistic at some point without any discretion to make reasonable adjustments.

This is a matter of considerable interest and importance. SBA has been reviewing this matter for some time. The relevance and validity of the New York prime rate is questionable. Testimony has been received by this committee on that very point. Therefore, Mr. Chairman, we feel it would be inappropriate to establish a rigid formula or base rate by legislation.

In this connection, the committee should be aware that we asked our National Advisory Council to chair a committee, including private sector resource people, to make recommendations to us in the area of interest rate policy. We expect to receive their report shortly.

Section 6 of the bill would require SBA to maintain a record of all applications for or inquiries about the availability of funding for financial assistance under the Small Business Act or Small Business Investment Act. The record is to be kept for 1 year from the date of application or inquiry.

We fail to see the utility of retaining records about all people who make inquiry concerning the availability of SBA funding and are concerned about the propriety of collecting such information. We currently retain records of applications for financial assistance

on an office by office basis for as long as those records are useful to us. We believe that such a utility test, as defined in the Paperwork Reduction Act of 1980, is preferable to a legislative requirement that records be retained for at least 1 year. Therefore, we do oppose this provision.

Section 7 of the bill would require SBA to notify the two congressional Small Business Committees before reprograming any program amounts authorized in appropriation acts or reports explanatory thereof, and before implementing any reorganization of the agency. It is already SBA policy to provide such notifications. We do not believe that such a provision should be enacted in law.

Sections 8 through 13 of the bill provide certain conforming and technical amendments to the Small Business Act. We do not object to their enactment. Section 14 of the bill requires SBA to adhere to the notice and comment rulemaking procedures of the Administrative Procedure Act in promulgating regulations relevant to establishing size standards, and we certainly do not oppose this requirement, although it is not necessary to state it in the Small Business Act.

Mr. Chairman, this concludes my prepared remarks. I would now be pleased to respond to questions.

Mr. MITCHELL. Thank you very much for your testimony. I lost count. Sometimes you were with us; sometimes you were against us; sometimes you were neutral and I lost count, but that is all right. In the back of my mind it appears that in general the administration opposes many of the recommendations contained in these two bills.

With reference to the Commerce Business Daily—first of all, let me say that in the hearing yesterday, we had 13 witnesses, representing all aspects of the small business community and as I recall, there was not a single witness who opposed any of the provisions in the two pieces of legislation we are discussing today. We had trade associations of broad representation, and most of them were very, very strong about the need for our Commerce Business Daily bill. There are several questions on this.

You indicated that Mr. Sowle is now making a commitment that he will enforce regulations in a slightly better fashion. One of the witnesses yesterday—I think it was Mr. Peterson, perhaps, it was Mr. Director—stated that there was some question as to whether or not Mr. Sowle had the power to enforce any such regulations.

But be that as it may, on page 2 you noted that the SBA surveillance reviews have consistently revealed over the years substantial noncompliance by contracting officers with regulatory CBD synopsizing guidance. Why do you now believe that this practice, which obviously has been in effect for many years, can now be revised and that advance notice can be afforded to small businesses which are desirous of bidding on Federal procurement opportunities? On what basis do you make the assumption that suddenly, magically, this transformation is going to take place?

Mr. SANDERS. Well, I think, Mr. Chairman, we do recognize and agree that there has been a problem. I think all we are asking here is that we give Mr. Sowle a chance to honor his commitment to respond in a timely fashion.

Mr. MITCHELL. Might I further indicate that I posed to some of the witnesses yesterday Mr. Sowle's proposition. They were very strong in pointing out that almost everything that they do must be done by mail and generally there is a 5-day lag because of the mail deliveries. When they make the bid or when they make the inquiry, very often they are at a point, by the time they receive the information back, where they have only 5 days in which to gear up to make sure that they are able to fulfill that contract. Every witness said that that was not sufficient time.

I think you are wrong on this one. I think that your position does not help the small business community. I would like to share your optimism about change, but I simply cannot.

Let me ask you a question about the economic opportunity loans. The administration has requested an increase in economic opportunity loans from existing levels of $60 million up to $100 million in fiscal year 1982 and $167 million in fiscal years 1983 and 1984. In past statements, the administration has used these higher numbers in order to assert that minority assistance is not being decreased even though the administration has proposed to eliminate the direct loan program.

Do you really have any reason to believe that it is realistic to project loans of $100 million or more per year, when the experience of this program through the first 6 months of this year shows an annualized year of less than $9 million, especially when it is considered that in recent years the program never exceeded a $25 million expenditure per year? On what basis is this astronomical increase assumed? The track record shows an annualized rate of $9 million for this year. Past years never exceeded $25 million and the administration is proposing $100 million in fiscal year 1982 and $167 million in fiscal year 1983. What was the basis for that assumption?

Mr. SANDERS. Mr. Chairman, would you permit me to refer this to the associate administrator who was in on the drafting of this and had probably some participation in the discussions at that time.

Mr. MITCHELL. Certainly.

Mr. SANDERS. Mr. Holloway, would you care to comment?

Mr. HOLLOWAY. Mr. Chairman, we are clearly going to have to make a very good effort with our regional Administrators, with our banking partners, and all involved in the system to improve our record in this area. The administration is desirous of maintaining a level overall of assistance to primarily minorities in the area of $410 million, which would be about 17 percent of the total budgetary authority available.

This is going to require quite an effort on our part and we have our job cut out for us, Mr. Chairman, and we are going to work on it.

Mr. MITCHELL. Well, it is more than quite an effort. It appears to be an almost superhuman effort. It appears that you are going to have to be Robin and Batman and Superman and everybody else, all rolled into one. You are talking about an increase in activity of over 150 percent. Again, I think it is unrealistic to project that kind of figure. I am not suggesting that people won't try very hard to reach it. But whenever we deal with goals and objectives they

have to be based on something, and, in general, we base them on past record or performance. I hope you are not suggesting that in the past the personnel at SBA were slothful and lazy and didn't produce, and that now you are going to make them produce. I don't think they were slothful or lazy. I just think it is unrealistic.

Let me raise just one more question and then I will turn to the other members for questions. This is on the SBIC authorizations. In earlier testimony this year, the SBA's acting Administrator supported the administration's budget request of $125 million for SBIC's in 1983. I understand that the agency has done a survey of SBIC's to ascertain their needs. What demand level did you ascertain for SBIC's?

Mr. SANDERS. Well, we felt that this amount would be adequate considering the refunding of the SBIC debentures. We made some calculations in our demands on that fund that probably come in the area of $75 or $80 million for those purposes and we felt that this would probably easily leave another $40 million for new start-ups and, based on historical evidence, that might provide for as many as 50 or 60 new SBIC's.

Mr. MITCHELL. Let me make sure I understand. Did your survey come up with a recommended figure of $75 to $80 million or was this in reaction to the $125 million ceiling imposed through the process in the executive branch? Was it the survey that you were referring to or your reaction to a dollar amount proposed in the executive branch?

Mr. SANDERS. We tried to calculate how much we would really be faced with in the refinancing of maturing SBIC debentures. I think that is the way we started off because we knew we would have to face up to it.

Mr. MITCHELL. Before you respond, Mr. Holloway, let me try to make it clear what I am talking about. If, indeed, a figure was given to you by OMB or through an interagency council or something like that of $125 million, then, obviously, you would plot your reaction to that figure. But that may or may not be the figure which would have appeared in your own independent SBA survey of SBICs to ascertain their needs. We are talking about two different things.

My question goes to this orange over here, not that apple. Whether or not the survey that SBA conducted enabled you to ascertain a demand level for the needs of SBIC's. That is the one that I am talking about.

Mr. HOLLOWAY. Mr. Chairman, the survey we conducted related primarily to the refunding situations. There are a total of some $150 million worth of debentures coming due during this fiscal year. There are some $35 million or so of those that are debentures of SBIC's in liquidation. We went to the companies themselves and asked them for their intent about refunding.

The total numbers that came back were approximately $90 million of indication of interest in refunding. We feel that on the normal credit evaluation and drop-out criteria, it will be around $75 million. It will accommodate the refundings. This will leave about $50 million for either new SBIC's or accommodating further requests for new money from existing SBIC's.

Mr. MITCHELL. $50 million?

Mr. HOLLOWAY. Yes, sir.

Mr. MITCHELL. Ninety from 125 is 35.

Mr. HOLLOWAY. Ninety was the raw figure. We feel actually about 75 to 80 of that will actually materialize. Not every request for funding is honored because of regulatory or other requirements at the time the request is made. We feel that is a realistic figure. Interestingly enough, we surveyed back from 1970 forward and since 1970 forward, the SBIC's draw down about 60 percent of the budgeted authority. So, they never really do draw down as much as they seem to think they will need up front. And, although the $125 million arguably may be somewhat lean, we believe it will be adequate.

Mr. MITCHELL. Thank you. Mr. Neal Smith.

Mr. SMITH of Iowa. Mr. Administrator, I want also to welcome you to the committee for your first appearance here and to assure you that I am very hopeful that you will get the agency perking a little better than I think it has been in the past. I, for one, want to cooperate in any way that helps small businesses and to be a vigorous opponent of whatever will hurt small businesses that can't be justified.

Before you became Administrator, a number of proposals in the last year and a half were sent to OMB and to the various offices in the administration, with regard to legislation and policy. Now, when you become Administrator, do you call those back or do you just, in effect, endorse those proposals? How do you handle that?

Mr. SANDERS. First of all, Congressman, I am pleased to see you here. We discussed some of these issues when I was still associate administrator in the management assistance area and I am anxious to follow up on some of those particular details now that I am in this seat.

In regard to your question, I have not, since I have been in this seat, had a single moment to go over to OMB and review all of the past history of our submissions and recommendations and the whole history of the evolution of the administration's final position respecting the Small Business Act.

I do intend to do that. I guess I am going to have to tell you that the reason that I haven't done it is I have had other priorities in readjusting personnel and getting——

Mr. SMITH of Iowa. Well, I can understand that, but failure to review those and make changes, if you deem it appropriate, in effect, amounts to an endorsement of those policies. And in the way things work around here, you become strapped with the position that was taken prior to your having an opportunity to review it. So, I assume that as soon as you can, you will review those and if you think they are not appropriate, try to get some change made.

Mr. SANDERS. I can tell you that I have had the opportunity, on a personal basis, to make my introduction to Mr. Wright, who is over at OMB now, having taken Mr. Harper's place. I do look forward to a fruitful relationship with him and you can be sure that in each instance I will press our recommendations as hard as I can——

Mr. SMITH of Iowa. Mr. Wright is the principal one at OMB who deals with the Small Business Administration?

Mr. SANDERS. I can't say that because we haven't gotten down to issues yet, but I think it is important for me to know every person at OMB that I——

Mr. SMITH of Iowa. It is interesting that you mentioned his name. So often over at OMB we can't find out who it is that handles the matters for different agencies. I know Mr. Wright and I hope that he is the one that SBA is primarily dealing with over there.

Mr. SANDERS. I think it is one of the jobs of the Administrator of this agency to try and see that each agency—in this case, mine being the Small Business Administration—has the best access it can at all levels of the administration, as well as up here in your committees.

Mr. SMITH of Iowa. One of my colleagues from Iowa is concerned about, and indeed we all are, the pollution control program. Let me ask you two or three questions that perhaps illustrate what we are talking about.

What has been the activity level in the pollution control program since OMB imposed the changes in January?

Mr. SANDERS. As you know, we sent back your letter to OMB in which you stated your position and the limits that you felt should be adhered to. I can tell you that last night I sent forward another letter to OMB, asking for reconsideration of several positions that we have taken and certain positions that we have studied in regard to both the level and the nontaxable aspect of the pollution control.

Mr. SMITH of Iowa. Well, has there been any activity since January?

Mr. SANDERS. You mean a change?

Mr. SMITH of Iowa. No; activity in the level of——

Mr. SANDERS. Oh, in the actual—I don't believe there has been, not at all.

Mr. MITCHELL. Will the gentleman yield? Some testimony yesterday on the pending pollution control bond guarantee applications stated that there were about 130 applicants prior to the announcement of the change. One of the witnesses stated that insofar as he knew only 2 people of the 130 had gone ahead with their request following the change. In short, we have lost 128 people. Now, is that accurate?

Mr. HOLLOWAY. Mr. Chairman, there are about 130 people. We went to the 130 people with a survey, asking that they indicate to us if they were interested in pursuing financing possibilities on a taxable basis. We received a total of 37 responses.

Mr. MITCHELL. Thirty-seven?

Mr. HOLLOWAY. Yes, sir. Thirty-two indicated that they would like to go forward on a taxable basis. Five indicated that they would not, and the others simply did not respond and I really believe they are just waiting to see what happens.

Mr. MITCHELL. Thank you for yielding.

Mr. SMITH of Iowa. That involves some $90 million. Is that correct?

Mr. HOLLOWAY. About $129 million.

Mr. SMITH of Iowa. $129 million of applications or dollars?

Mr. HOLLOWAY. Dollars.

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Mr. SMITH of Iowa. All right. The Mitchell bill, would change the word "may" to "shall" as it applies to tax-exempt pollution control financing, but you are opposed to that bill. Wouldn't this help you at OMB? I mean, then you wouldn't have to fight with OMB. I don't understand why you oppose the bill.

Mr. SANDERS. You don't really expect me to answer that.

Mr. SMITH of Iowa. I take that answer as meaning you really are for the bill.

That is all I have, Mr. Chairman.

Mr. MITCHELL. Thank you, Mr. Smith.

[Additional testimony of Small Business Coalition for Pollution Control follows:]

THE SMALL BUSINESS COALITION FOR POLLUTION CONTROL,
Washington, D.C., May 5, 1982.

Representative PARREN J. MITCHELL,
Chairman, Committee on Small Business,
House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: This letter is in furtherance of this Coalition's testimony before your Committee on April 28 with respect to H.R. 6086, a bill to amend the Small Business Act and the Small Business Investment Act, and is in the nature of an amplification on testimony offered before your Committee on April 20 by representatives of the Small Business Administration, specifically Mr. James C. Sanders, Administrator, and Edwin T. Holloway, Associate Administrator for Finance and Investment.

During a colloquy with Administrator Sanders during the questioning period following the presentation of the Administrator's prepared statement, you asked the Administrator:

"Mr. MITCHELL. Will the gentleman [Mr. Smith] yield, because this is some testimony we heard yesterday and it was suggested that in the pending pollution control bond guarantees applications there were about 130 applicants prior to the announcement of the change and it was further suggested by one of the witnesses that insofar as he knew only two people of the 130 had gone ahead with their request, following the change. In short we have lost 128 people. Now, is that accurate."

Associate Administrator Holloway responded:

"Mr. HOLLOWAY. Mr. Chairman, there are about 130 people. We went to the 130 people with a survey, asking that they indicate to us if they were interested in pursuing financing possibilities on a taxable basis. We received a total of 37 responses."

In response to your query "37?," Associate Administrator Holloway continued:

"Mr. HOLLOWAY. Yes, sir. Thirty-two indicated that they would like to go forward on taxable basis. Five indicated that they would not and the others simply did not respond and I really believe we are just waiting to see what happens."

This testimony of Associate Administrator Holloway is accurate. It is not, however, complete, and the complete information with respect to the status of these applications should be helpful to the Committee in ascertaining precisely where the program now stands.

This additional information is as follows: Following the receipt of the thirty-two responses indicating that those applicants wished to pursue the guarantee on a taxable basis, SBA sent an additional letter to those applicants. Six to eight of those applicants responded that they wished to proceed; however, the remaining twenty-four to twenty-six applicants either did not pursue the matter further by responding to the second letter or indicated that they were not prepared to proceed at this time. Among those six to eight responding, further, no guarantee has been closed, principally because of the severe interest rate problem faced by these applicants in pursuing the taxable basis alternative. Thus, in summary, although some applicants did indicate an interest in going forward on a taxable basis, about one out of five applicants pending, none has, in fact, done so to the point of closing a guarantee.

We think this additional information shows conclusively that the OMB requirement that the program proceed on only a taxable basis has rendered it inoperable.

We respectfully request that this letter be made part of the permanent hearing record with respect to the April 28–29 hearings.

Respectfully submitted.

RANDAL C. TEAGUE.

Mr. SMITH of New Jersey. First of all, I want to welcome Mr. Sanders to the committee. I think it is a credit to him that he has had a remarkable small business success story. I think most people are aware of that and it is good to have a person with that kind of background, who understands the needs and concerns of small business, at the helm of the SBA.

I would also like to thank Mr. Templeman for keeping the ship afloat in the interim process and I think he did an outstanding job.

I have a couple of questions, one with regard to loan availability. Mr. Administrator, we have heard conflicting reports about the availability of direct loans. Some of the offices throughout the country are reporting that they don't have the money to lend and, yet, we hear demand is low. I wonder if you could clear up for us what the level of availability is with the direct loans.

Mr. SANDERS. The loan demand is down all over, not only in SBA, but in other financial institutions. But we attribute this largely to both the slow economic conditions, the recession, and the high interest rates. If you would like some numbers on that, I think maybe Mr. Holloway might have some percentages.

Mr. HOLLOWAY. Congressman, in the direct area, in the first 6 months of the fiscal year, we have used, out of $120 million, we have used about $40 million. In the guarantee area, out of about $2.3 billion, we have used $708 million. So, we are around 35 to 40 percent, instead of 50 percent, as we are halfway through the fiscal year. We do anticipate and hope for a bouncing back of the economy and some pent-up demand to be released when interest rates recede somewhat.

Mr. SMITH of New Jersey. Have any of the offices been told that there isn't any money available at this point?

Mr. HOLLOWAY. We are constantly fighting those types of reports. We have put out a number of notices to our field offices. We have encouraged them to make known the availability of the funding, both direct and guarantee. We have made known to them in formal instructions the flexibility that we have to switch money from one region or one district to another region or another district to accommodate the needs that are there. I just have to deal with those situations on the basis of specifics, Congressman, because if I can identify the person out there that is saying that there is not any money available, I certainly think that you and I would agree that I should straighten that out.

Mr. SMITH of New Jersey. Thank you.

Second question: Several parts of the SBA loan portfolio suffer from extremely high default rates. I wonder if you could share with us briefly what those areas are in which this problem exists and also what is being done at this point to try to improve that situation.

Mr. SANDERS. Associate Administrator Holloway, as you know, has the finance and investment section, but, as you know, our default rates in the direct loan area are greater than they are in the guaranteed loan area. That kind of ratio continues and maybe if you would like some more—is that——

Mr. SMITH of New Jersey. I would appreciate for the record if you could detail that. It would be very helpful.

Mr. HOLLOWAY. We are making an effort, Congressman Smith, to assure that we are administering the programs in a way that meets the statutory requirement of reasonable assurance of repayment. We firmly believe that we are not helping anybody if we try to create an artificial achievement record of making more loans than we professionally believe can be repaid. We have a number of indicators that tell us that we should do a better job of assessing the risks involved.

For example, in the economic opportunity loan program, the rates of trouble there are now around 41 percent nationwide. That is, the loans are either in default 60 days or more or they are in liquidation. That is up from around 34 percent a year ago. In our guarantee area, our repurchases of loans have more than doubled in the past 15 months, up from $20 million a month to some $53 million a month. So, we have the indicators there that we really haven't been doing the job that we ought to be doing in terms of helping people.

The need for money that people have is certainly there, but it is not always a need for money on the condition that they pay it back or they talk to the judge about it and it is that part of it that we are trying to do a better job of.

Mr. SMITH of New Jersey. What is done with the troubled loans?

Mr. HOLLOWAY. We work with them, provide servicing in our portfolio management area. We leverage in our management assistance capability, both the in-house capability and the capability of SCORE and ACE and other private sector resources and try to help people. That is where we are coming from in the program. It is a long way from the making of a loan to the creation of a successful small business and that is our real challenge, as we see it, and we know if we create successful small businesses, we will get repaid. It is when they can't pay, that they don't pay.

Mr. SMITH of New Jersey. Do we have sufficient personnel in the SBA who are able to marshal all those forces together in the district offices throughout the country?

Mr. HOLLOWAY. We are attempting to increase our productivity and get the job done and I believe through leveraging the private sector better, by more delegation to banks and our other lending partners that we can get the job done within available resources.

Mr. SMITH of New Jersey. Thank you. I yield back to you.

Mr. MITCHELL. Will you yield to me for just a moment?

Mr. SMITH of New Jersey. Certainly.

Mr. MITCHELL. All of us are concerned about the defaults, but to what extent does the increase in defaults reflect the economic vicissitudes that the entire Nation is confronting. These are your high risk loans initially and obviously with the economy being in the shape that it is in—we hope that it will improve—but it would seem to me that the general economic conditions would impact more heavily on your high risk loans than they would on others. We see businesses not at all associated with SBA filing bankruptcies in astronomical numbers. So, does any of that default—the increase that has occurred over the last year, which you just alluded to—reflect the state of the economy, the depressed economy itself?

Mr. HOLLOWAY. It is a substantial factor, Mr. Chairman. The condition of the economy right now in a recession is a factor and it is

causing many people to defer borrowing wherever they can in banks that have nothing to do with SBA programs.

Mr. MITCHELL. I am not talking about coming in to borrow. I am talking about those who have borrowed and are not able to repay and that are in trouble. It seems to me those are the ones that are equally impacted.

Mr. HOLLOWAY. It is a substantial factor.

Mr. MITCHELL. Thank you. Mr. Hiler.

Mr. HILER. Thank you, Mr. Chairman.

Mr. Sanders, I have several questions. Before I say that, I might preface my first question with another question. Did you see the article in the St. Louis paper? It was a series of 10 articles that were run late August, early September, about the default rate of the direct loan program?

Mr. SANDERS. Yes.

Mr. HILER. Didn't that article seem to indicate—and you can respond to that—but I believe the article indicated that the default rate on the direct loan program has not been something that has cropped up in the last 6 months, but, in fact, has been a prevalent part of the program for the last 10 years?

Mr. SANDERS. I believe it is historical, yes. I know of no contradiction to that.

Mr. HILER. So, there is nothing new in that there is a default rate on SBA loans.

Mr. SANDERS. That is right. That ratio of a higher default rate in the direct loans, I think, has been historical and always existed.

Mr. HILER. Thank you. You have commented in your testimony on H.R. 6086 on section 2 about the provision that would require the SBA to operate all of its guarantee programs in the full amounts provided by law. Could you describe again the kinds of problems that can create?

Mr. SANDERS. We feel, of course, that we must have a flexibility to respond to changes as such. We feel that this provision would take away the flexibility to manage and, I think, that puts it about as plainly as we can. We just oppose the rigidity here.

Mr. HILER. And your feeling is that if this section were included and passed into law, in H.R. 6086, that it would create a situation where the SBA might be granting loans or loan guarantees or surety bonds or whatever on a noneconomic basis, but would instead be doing it just to comply with the law that you have to use up all your money?

Mr. SANDERS. We wouldn't like to be put in that position. That is correct.

Mr. HILER. It is a dangerous position to put someone in who is supposed to be providing management assistance. Isn't it?

Mr. SANDERS. Yes, that is right.

Mr. HILER. Thank you. I also had a question on section 6 of the bill which would require SBA to maintain a record of all applications for or inquiries about the availability of funding for financial assistance. How do you interpret that section?

Mr. SANDERS. We are trying to measure the effectiveness of some of these activities, but I think this is not the way to do it. Part of the problem in analyzing the full operations of the SBA agency is to try to weed out a lot of the duplicative reporting paperwork. We

have a lot of paperwork problems in the agency. I think if you are going to try and measure certain things like this, a much more effective technique would be the one that was proposed in the Paperwork Reduction Act, the so-called utility test or shopping. You move in and you make a test of the kind of response you are going to get by sending in a professional type person to measure this kind of thing. I think you will get better results that way than you will by adding another burden of reports on the personnel in the SBA who are already overburdened with a number of reports they have to prepare and which prevent them from dealing with the problems about them.

Mr. HILER. What kind of record requirements do you have now? What is typical? If I called up on the phone and said, gee, my name is John Hiler and I would like a loan and you say, fine, come in and see us and I never come in and see you. Is that logged in that someone had called?

Mr. SANDERS. I don't know that, Congressman. Maybe the Associate Administrator knows if we keep a record of just a telephone call.

Mr. HOLLOWAY. Congressman, we do keep an inquiry record of either phone calls or walk-ins to talk about loan assistance. That record is maintained for as long as we need it, but generally about 1 year in the field office where it is used. If you came in a second time, the first thing the receptionist does when she finds out your name is Mr. Hiler is to see if Mr. Hiler has been in before, and gives the information to the loan officer. He sees what we told you the last time and updates it for what we are telling you this time. So, we do have that type of documentation that is maintained in the local offices. It is not centralized or computerized in any way, but it is just there where it is thrown away when we no longer need it.

Mr. HILER. I have one other question concerning the loan extensions. Last year in the Reconciliation Bill, we adopted a change in the loan program, which was designed to enable SBA to extend the term of a loan so as to reduce the monthly payments by borrowers. We intended this to provide relief where appropriate to small businesses which were unable to handle the high repayment necessitated by very unprecedented high interest rates that developed over the period from 1977 to 1981. However, SBA has interpreted this language to require that any extension of the repayment period be accompanied with an increase in interest rates to their unprecedented highs that were inherited when the former Administrator took office.

The result has been higher loan repayments instead of the lower payments we had intended. I guess I have two questions. One, why has SBA been unwilling to extend the terms of the loans as authorized in Public Law 97-35 or in the way we originally anticipated?

Mr. HOLLOWAY. Congressman, I think there is some confusion here. We are making every effort to get the banks involved to extend these loans. If a small business has a lower interest rate loan, as an example, we have within our power the ability to approve either deferments or reamortization as a result of extending the term. The problem we run into is where the request is for a total restructuring of debt and, in fact, a total refinancing. The

way we try to do it is to leave—if we have 12-percent money on the books—to leave the 12 percent money on the books and accommodate any additional needs with a second loan, if necessary, which must be made at whatever rate the bank will make it available.

So, we are attempting to deal with that issue in that way, but the statute itself really does not require the bank to make a new loan at the old interest rate.

Mr. HILER. Mr. Chairman, could I defer to minority counsel to ask a question?

Mr. MITCHELL. Certainly, there is no objection.

Mr. WITTIG. To clarify the issue, when a small business with an existing guaranteed loan has come to the Small Business Administration through his bank requesting an extension of the term and a reamortization of his payments, the Small Business Administration's General Counsel has ruled that that may not be accomplished unless the small business is willing to take higher interest rates.

Mr. HOLLOWAY. A totally new loan would have——

Mr. WITTIG. Let me rephrase it. This is not a new loan. Where a small business with an existing Small Business Administration guaranteed loan requests under the statute to have his term extended and thus his payments reamortized because the term is longer, as authorized by the statute, the Small Business Administration General Counsel has ruled that that cannot be accomplished as the statute directs without interest rates being raised.

Mr. HOLLOWAY. Mr. Chairman, may I submit an explanation of that for the record? Counsel is not familiar with that particular opinion and it may relate to some unique special circumstances that we are not aware of.

[See attached letter and supplementary question 8, following:]

MAY 5, 1982.

Mr. RAYMOND S. WITTIG,
Minority Counsel, Committee on Small Business,
House of Representatives, Washington, D.C.

DEAR MR. WITTIG: At a hearing held on April 29, 1982, to discuss H.R. 5551 and 6086, you stated that you had been advised of an opinion of the General Counsel of the Small Business Administration regarding the granting of extensions of the terms of business loans the repayment of which are guaranteed by SBA. You stated that this opinion held that if such an extension were granted, SBA would not object as a matter of law to the imposition by the participating lender of a higher interest rate for the remaining term of the note which evidenced the loan transaction, notwithstanding the provisions of subsection 7(a)(3) of the Small Business Act.

Please be advised that no such opinion of the General Counsel exists. Any information which you may have received to the contrary is in error. If you have a written opinion expressing such a position, I would appreciate your furnishing a copy to me.

As you know the facts surrounding a given guaranteed loan are crucial to determining the applicability of any of the provisions of the Small Business Act or SBA's regulations to that loan. If you have a certain fact pattern in mind, and you would like to have an advisory opinion of the applicability of the Small Business Act or the regulations to those facts, please furnish me with a statement of those facts, and I will be pleased to respond as soon as possible.

Sincerely,

ROBERT B. WEBBER,
Acting General Counsel.

SBA RESPONSES TO QUESTIONS FROM APRIL 29 HEARING

Question 1. Section 6 also requires SBA to obtain information from any person who inquires about SBA assistance. In your judgement, could this become a deterrent to businesses which might perceive SBA as insensitive or overly bureaucratic? Would businesses be discouraged from even making inquiries because of the knowledge that they would be required to submit this information to SBA?

Answer. We do not believe so in the case of appl ations. This information would be included in that which would be provided when an application was made anyway. It is possible that those making an inquiry by phone, or even in person, might object to being so questioned when they may have only been seeking information from SBA.

Question 2. The Administration has proposed an increase from $60 million to $167 million in the Economic Opportunity Loan guarantee program. Current annualized demand for that program is $8.8 million. What leads you to believe that you will be able to generate a program at the proposed level? How much of these funds will lapse at the end of the fiscal year?

Answer. The proposed level is based upon contemplated recovery in the economy. If that recovery did not occur, it is true that the increase would not be necessary.

The proposal of $167 million in loan guarantees for the Economic Opportunity Program was intended to help alleviate the impact on the minority small business community due to the elimination of direct funding in fiscal year 1983. The actual minority lending in fiscal year 1981 amounted to $414 million, excluding MESBIC lending. This included $147 million in direct loans. In order to ensure a comparable supply of funds for fiscal year 1983, the guaranty level for Economic Opportunity Loans was adjusted upward accordingly.

Projecting the current demand for Economic Opportunity guaranty loans, there will be approximately $90 million in unused program authority lapsing at the end of fiscal year 1982. This decline in demand is due mainly to present economic conditions and is not interpreted as an indication of a decrease in future minority lending demand.

Question 3. What is the status of SBA's study of the proper loan guarantee interest rate ceiling?

Answer. The Agency has sought additional recommendations on interest rate ceilings from a sub-committee of the SBA National Advisory Council. A preliminary report has been provided.

Question 4. In testimony before this subcommittee yesterday, Robert Schiffer, representing the Public Securities Association advocated complete elimination of the interest rate ceiling. He contended that if this were done, market forces would drive guarantee interest rates down since there would be no psychological tie to the ceiling. What is your reaction to this argument?

Answer. This of course is one of the options open to the Agency. We think it is a suggestion worthy of study.

Question 5. What is the status of the proposed size standards revision? What do you expect will be the time consumed before final regulations are published? Will SBA prepare a regulatory flexibility analysis of the size standards even though your General Counsel has ruled that one is not required?

Answer. An Advance Notice of Proposed Rulemaking to revise the SBA size standards was published in the Federal Register on May 3, 1982. This notice provides for a 90-day comment period to assess the public's reaction to the proposed changes. This would then be followed by additional changes, where justified, in the form of a proposed rule. Following normal administrative procedures, SBA expects to publish a proposed rule in the fall and a final rule in the first half of 1983.

A regulatory flexibility analysis is required for rules that have "a significant economic impact on a substantial number of small entities." SBA will perform such an analysis to determine the magnitude of impact and the number of small entities affected. This analysis will be available at the time of the proposed rule.

Question 6. It is my understanding that SBA has proposed interim changes in size standards until a permanent revision has been approved.

What is the status of this proposal?

Answer. In January of 1982, SBA submitted a proposal to OMB for an interim change that would have increased all dollar volume size standards by 25 percent. This proposal has been dropped. To have interim changes at the same time as the present advance notice would cause confusion.

Question 7. Although Congress authorized a $250 million Pollution Control guarantee program, OMB only allowed SBA to spend at a $150 million rate while it sent a rescission request to Congress. That rescission has been disapproved, and I under-

stand that SBA has requested an additional allotment from OMB so that it can spend at the Congressionally mandated level. What is the status of that allotment?

Answer. The allotment for the pollution Control Financing Guarantee Program is the subject of present negotiations between SBA and OMB.

Question 8. Loan extension: Last year, in the Reconciliation Bill, we adopted a change in the loan program which was designed to enable SBA to extend the term of a loan so as to reduce the monthly payments by borrowers. We intended this to provide relief, where appropriate, to small businesses who are unable to handle the high interest rates. However, SBA has interpreted this language to require that any extension of the repayment period be accompanied with an increase in interest rates to their unprecedented highs. The result has been higher loan payments, instead of the lower payments we had intended.

(a) Why has SBA been unwilling to extend the terms of loans as authorized in P.L. 97-35?

(b) In the light of the statutory language which refers to extension and refinancing of loans, would you be willing to consider changing SBA policy to allow loan extensions (as opposed to refinancings) without a change in the interest rate?

Answer. (a) Not only is it untrue that SBA is unwilling to extend loans as authorized in P.L. 97-35, but SBA was willing to, and did extend loans under different authority prior to the passage of P.L. 97-35. The Agency remains willing to extend loans upon a showing that such extension is necessary to effect orderly repayment of the obligation.

(b) As stated in (a) above, no change in policy is required to allow extension of loans without a change in interest rate.

Question 9. Small Business Investment Companies: Mr. Sanders—If the SBIC authorization were increased to $250 million from $160 million, would there be sufficient demand for the funds?

Answer. Based on previous demand and current conditions, it appears there would not be sufficient demand.

Question 10. Mandatory Spending of SBA Funds: (a) There has been information that SBA District Offices have discouraged potential direct loan applicants from applying for funds. A comparison of last years expenditures vs. annualized expenditures through March of this year indicates that ½ the direct loans and ⅓ of the guaranteed loans will be made in 1982 as were made in 1981. Loan interest rates for guaranteed loans did not significantly increase for guaranteed loans. What accounts for this difference?

(b) What directives has the SBA received from OMB to reduce outlays?

(c) What are the spending levels by program that OMB has required you to meet?

(d) Absent this kind of legislation, what would you propose to prevent an ad hoc reduction in loan approvals by SBA at the direction of OMB?

Answer. (a) Neither OMB nor SBA Central Office have discouraged application for direct loan assistance. To the contrary, SBA Central Office has instructed all field offices not to discourage qualified applicants but rather if they are short of funds to request additional funds by transfer from another location. With regard to the drop in loan guaranty volume this year as compared to last, it is becoming more clear every day that potential borrowers are very hesitant to borrow in the present questionable economic climate. This is particularly true of those whose needs are discretionary. They simply are electing not to borrow at high interest rates to expand when they are not at all sure that they will be able to profitably expand sales.

(b) The Small Business Administration receives its budget authority and outlay directives from OMB in the form of an Allowance Letter. This outlines the Administration's recommendations for the current year and the budget year as well as guidance for the outyear budget estimates.

(c) The spending levels for fiscal year 1982 and fiscal year 1983 are as follows:

[Dollars in millions]

Programs	Fiscal year 1982		Fiscal year 1983	
	B/A	OL	B/A	OL
Salaries and expenses	$222	$241	$228	$244
Business loan and investment fund	326	359	144	130
Disaster loan fund		−77		−290
Pollution control		−17		−19

Programs	Fiscal year 1982		Fiscal year 1983	
	B/A	OL	B/A	OL
Lease guarantees	3	3	7	3
Surety bond	19	16	.....	10
Total	570	525	379	78

(d) Under the 1974 Budget and Impoundment Act, a process was established that recognized the fact that between the time an Appropriation Bill is enacted and when expenditures are to be executed that priorities and economic conditions could change. In order to accommodate this change, a deferral and/or rescission process was established. Such is the case now and as a result, the Administration has requested several deferral actions relevant to SBA's programs. Presently there are two pending deferral actions.

(1) Business Loan and Investment Fund: Reduce Guarantee Loans from $3.3 billion to $2.735 billion.

(2) Surety Bond Guarantees Revolving Fund: Reduce bond guarantees from $1.2 billion to $1.08 billion.

Question 11. Surety Bond Eligibility Criteria: (a) The SBA recently relaxed the eligibility criteria for surety bonds. The previous standards, if continued all year, would have cut program expenditures in half. Did the savings during the first half of the year have any impact upon the SBA's decision to return the standards to previous levels?

(b) To what extent were the previous standards related to OMB's direction to you to reduce program expenditures?

(c) Did the SBA determine, before it relaxed the standards, that reduced demand due to the recession would make expenditure-controlling restrictions unnecessary?

Answer. (a) At approximately the same time SBA issued its budget restraint memorandum of January 15, 1982, the effects of the business downturn and an unusually bad winter were beginning to be felt nationwide. While it is difficult to designate any specific cause, the impact on the Surety Bond Guarantee Program, in any case, was noticeable and effective April 1, 1982, the standards of the January memorandum were relaxed.

(b) The advice from OMB was to practice budget restraints in all programs to the extent possible via administrative action. The SBG underwriting criteria published by seven memoranda beginning March 27, 1981, were in compliance with that request.

(c) The adverse effects of the business downturn on small business as well as the extreme winter played a major part in the decision to relax the standards.

Question 12. Codification of Loan Guarantee Spread Rates: (a) Some have suggested that any recent SBA regulatory changes have been directed by OMB. What would prevent OMB from ordering you to change guarantee loan interest rates to discourage bank participation in the program?

(b) What suggestion do you have to avoid an attempt by OMB to further restrict SBA programs?

Answer. (a) No such regulatory changes in interest rate spread or ceiling rate have been suggested by OMB. In fact, no such changes have been made. A proposal for change was made simply because of the Agency's view and the view of at least two congressional subcommittees, that interest rates were too high. In the face of adverse comments to the proposal, no change was made.

(b) We see no need for a mechanism to avoid something that has not happened and is not contemplated.

Question 13. Reprogramming Notice: For the first time, although spotty, the SBA has notified the Minority of reprogramming actions. Should we be concerned that privilege now granted might be revoked?

Answer. As a matter of courtesy, the Agency has been informing the Small Business Committees of proposed reprogramming actions.

Mr. HILER. I would just like to close, Mr. Sanders, by saying that I have a SBA office right across the hallway from my office in South Bend and I have found your people there to be most professional and most helpful and we have a great amount of dialog between the two offices. I just wanted to let you know there are some folks in South Bend doing a good job for you.

Mr. SANDERS. Thank you.

Mr. MITCHELL. I have a few more, just little housekeeping questions, that I would like to ask.

We were talking about the recordkeeping. I have been on this committee for 12 years. In all those years the Administrator or the officials have come in to testify that they don't have the ability to project program demand because they don't keep records on certain things.

On page 8 of your statement the agency opposes any provisions to require recordkeeping on what amounts to inquiries about funding which would facilitate the projection of demand. Something, again, miraculously changed when for 12 years we have heard we can't do any projections because we don't have the records. You say that records are kept well. Let's try something out for today.

It is my birthday. Would you give me a little gift? Would you send to me by Tuesday a copy of each telephone inquiry received by SBA, by the district or branch office, that was received on my birthday today. Just the telephone inquiries relating to the availability of loan funds or the guarantees. Could you do that?

Mr. HOLLOWAY. Mr. Chairman, we will certainly do it. It will have to come in from 95 different offices and I don't know that we will have it by Tuesday, but when we go back today, we can request that information be sent in.

Mr. MITCHELL. I will accept a part of a birthday present, rather than a total one. Do your best.

Mr. SANDERS. We will start that right away, Mr. Chairman.

Mr. MITCHELL. Thank you so much and we can get something pretty definitive by Tuesday, right?

Mr. SANDERS. I think you will have some indication by Tuesday. I am sure that every person in the field is going to be interested in responding to your request, particularly on your birthday.

Mr. MITCHELL. Let me go back to the pollution control issue. You said you surveyed approximately 130 people and of that number 32 replied to your survey. Right?

Mr. HOLLOWAY. No, 37.

Mr. MITCHELL. OK, 37, and 5 were negative. They weren't interested, and 32 said that they were interested. Have the 32 people reapplied? That is the acid test.

Mr. HOLLOWAY. They really were not asked to reapply, Mr. Chairman. We asked them if they were interested in pursuing the matter on a taxable basis to refigure their needs, work with their financial institutions and brokers that were involved and furnish us the information necessary for us to make a determination.

Mr. MITCHELL. Your survey didn't advise people if they were interested that they would have to reapply?

Mr. HOLLOWAY. We are not requiring them to reapply. We are just requiring them to submit additional analysis.

Mr. MITCHELL. No, no. That is not quite what I am saying. It would seem to me that as a part of that survey, you would have said if you are interested it will be necessary for you to reapply. You didn't do that?

Mr. HOLLOWAY. We didn't ask them to reapply. We asked them to furnish additional information.

Mr. MITCHELL. Then, in short, we still have 130 people out of the program as of right now. Not in the program simply because or partially because of the change in regulations, right?

Mr. HOLLOWAY. The interest on the part of most of those people is believed to still be there.

Mr. MITCHELL. On the part of the 32?

Mr. HOLLOWAY. We did not get responses from the majority of the people, but they have not withdrawn their applications. The matter is somewhat fluid and they are waiting to see what happens.

Mr. MITCHELL. That is one way of interpreting it. I just wouldn't make that interpretation.

I have just a few more questions.

I was very glad to hear your testimony on your direct loan program, when you pointed out that time and time again you tell your field people that money is there. If it is not available in this region, we can shift it, that kind of thing. Yet, the data that I have before me is very disturbing. There are 10 Small Business Administration district offices that have not approved a single 7(a) direct loan in the first 6 months of this year, 10 of them without one 7(a) direct loan approved. There are 32 SBA district offices which have not approved any EOL loans in the first 6 months of this year. Have you contacted these offices? Were you aware of this?

Mr. HOLLOWAY. Yes, sir, we are aware of that and are in ongoing communication with the regions and the districts. Of course, 16 percent money is a part of the problem; 15 5/8 is our rate right now and many businesses have a hard time turning a profit, say, of 20 percent on money and 16 percent is going to the loan——

Mr. MITCHELL. You have contacted offices that I mentioned to find out why not a single dollar has been made under either of these two programs and the response from those offices is that people don't want to borrow at that rate?

Mr. HOLLOWAY. The interest rate is believed by us to be a major factor, Mr. Chairman.

Mr. MITCHELL. That is the national office. Have you contacted them at the district office to find out why they haven't made a single loan? It may be that there is something that is not related to the interest rate.

Mr. HOLLOWAY. One of my deputies surveyed yesterday afternoon some field offices to get a feeling on this and in a number of these one loan would practically use up the allotment they have in the EOL program.

Mr. MITCHELL. Well, what about the 7(a) direct loans? That money is available.

Mr. HOLLOWAY. The money is available. We are, Mr. Chairman, meeting the legitimate demand that is there for this type of money that meet the criteria.

Mr. MITCHELL. Believe me, I am not doubting your word, but when we deal with a total of 32 offices or more where not a single dollar has been spent in the first 6 months of this year under either loan program, it seems to me something is wrong, even taking cognizance of the fact that the interest rates are high. But that almost suggests closed programs.

Mr. HOLLOWAY. Mr. Chairman, these offices have not been told. It has not been suggested to them that they are not to meet the legitimate demand that is there.

Mr. MITCHELL. Is it possible that these offices are pushing for the guarantee program, rather than the direct loan program? As I understand it, guaranteed loans are being made and those interest rates are even higher than the interest rates on these two programs.

Mr. HOLLOWAY. That is correct. We are encouraging the use of the guarantee program as required by statute; as long as the guarantee loan is available, we really don't get down to the direct money. So, that is the program we talk about first.

Mr. MITCHELL. Then, perhaps, it is an overemphasis on the sell of the guarantee program that is a factor you have to reckon with, in addition to the interest rates.

Mr. HOLLOWAY. We will certainly stress that in our future communications with the field offices, Mr. Chairman.

Mr. MITCHELL. The House is now in session. I assume they are doing the 1-minute speeches. I don't want to prolong the hearing. I do have additional questions that I would like to submit to you and I will try to get them to you right after I receive the information on next Tuesday. Then I will shoot my questions out to you. All right.

Gentlemen, thank you very much.

Mr. HILER. Mr. Chairman, I might have additional questions to submit for the record.

Mr. MITCHELL. Of course, and I would ask unanimous consent that all members be allowed to submit additional questions for the record.

Gentlemen, thank you very much. It is a pleasure to have had you here.

Mr. SANDERS. Mr. Chairman, I would like to thank you for you courtesy and all of your for your comments and, incidentally, I appreciate some of the points you brought up. You can be sure that I will get back and try to find out some of the answers. I like that kind of support and when you have some problems that come up and we find out about them, maybe we will correct part of the operation. We would like to have it run smoother.

Thank you.

Mr. MITCHELL. Thank you very much.

This hearing is now adjourned.

[Whereupon, at 11:13 a.m., the subcommittee adjourned, to reconvene subject to call of the Chair.]

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